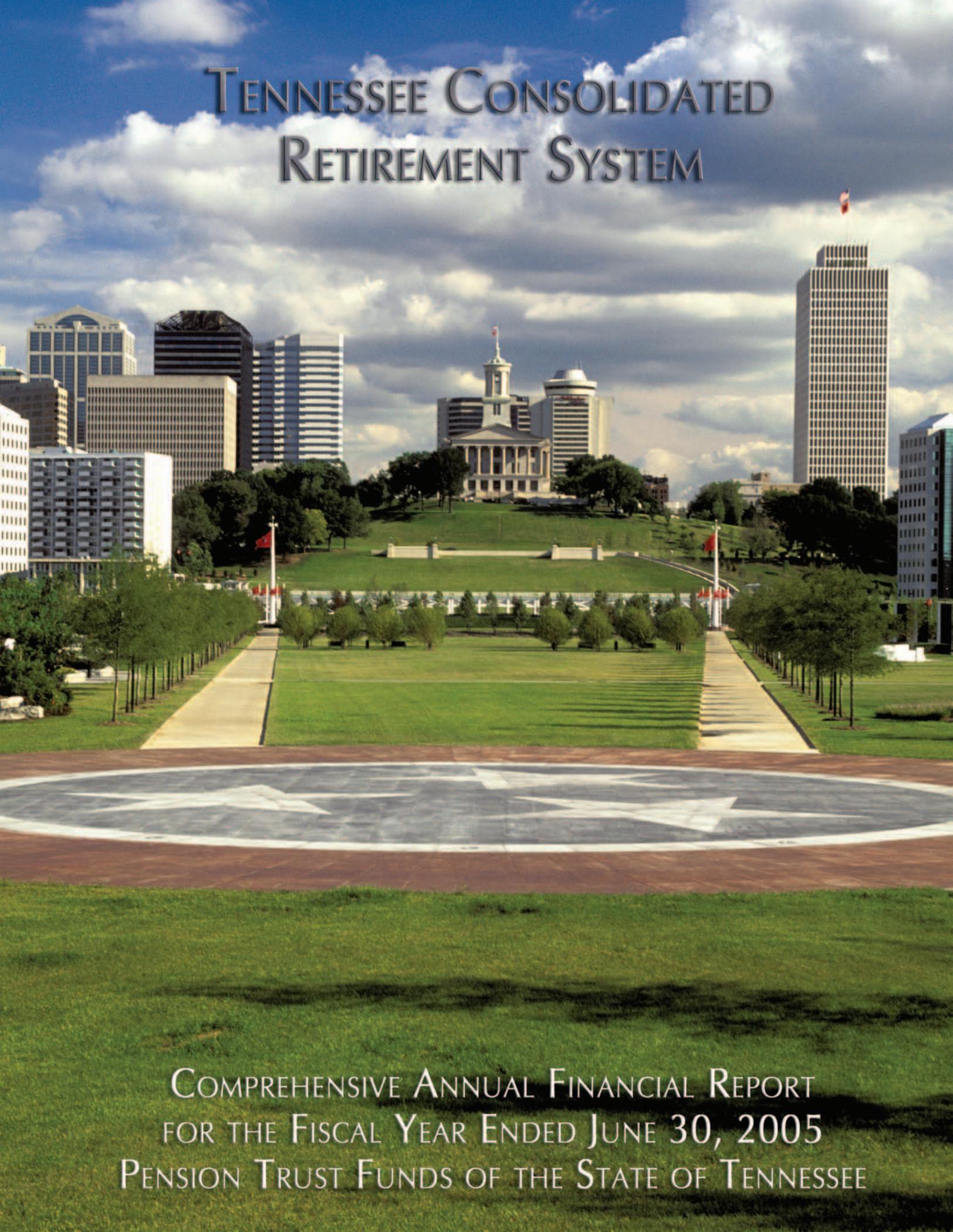
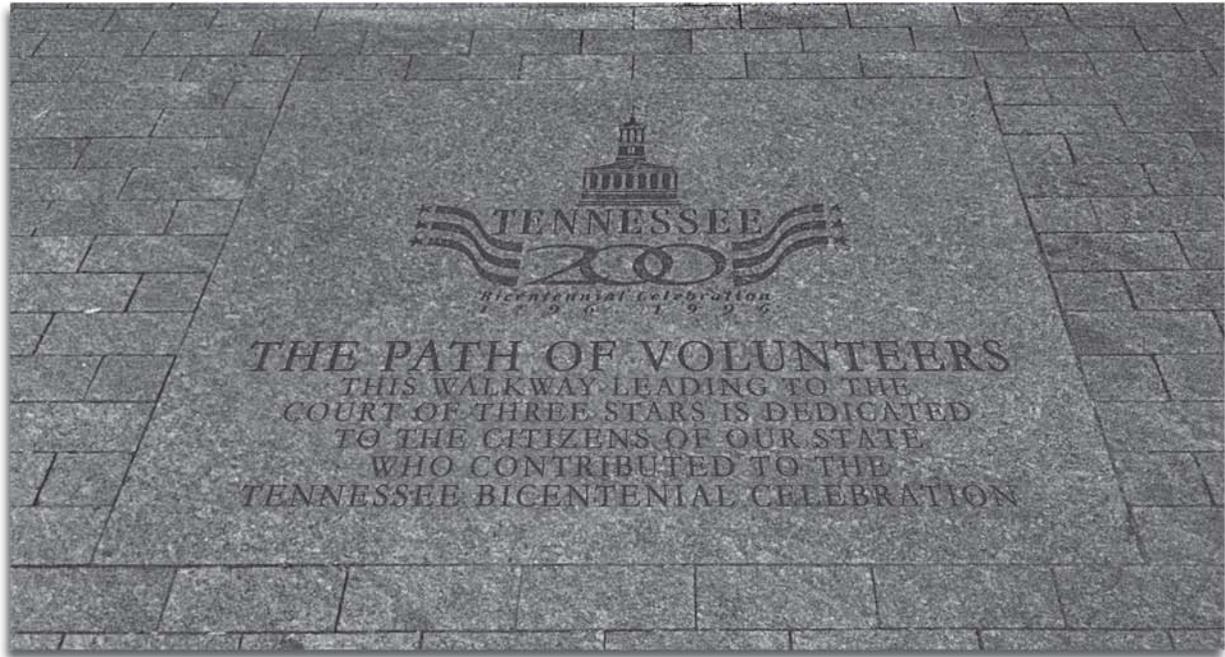


TENNESSEE CONSOLIDATED RETIREMENT SYSTEM



COMPREHENSIVE ANNUAL FINANCIAL REPORT
FOR THE FISCAL YEAR ENDED JUNE 30, 2005
PENSION TRUST FUNDS OF THE STATE OF TENNESSEE

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM



FEATURING PHOTOGRAPHS OF THE
TENNESSEE BICENTENNIAL MALL STATE PARK

COMPREHENSIVE ANNUAL FINANCIAL REPORT
FOR THE FISCAL YEAR ENDED JUNE 30, 2005
PENSION TRUST FUNDS OF THE STATE OF TENNESSEE

Prepared by: State of Tennessee Treasury Department
10th Floor, Andrew Jackson Building
Nashville, Tennessee 37243-0230
(615) 741-7063
www.treasury.state.tn.us/tcrs
Dale Sims, State Treasurer
Jill Bachus, TCRS Director

Bicentennial Capitol Mall State Park

The Bicentennial Capitol Mall State Park is located in the shadow of the State Capitol. The 19-acre park is designed to compliment the Capitol, give visitors a taste of Tennessee's history and natural wonder, and to serve as a lasting monument to Tennessee's Bicentennial celebration in 1996.

The park includes a 200-foot granite state map which highlights the major roads, 95 counties, rivers and other interesting geographic formations and details of each county. A Railway Trestle stands as a reminder of the importance of railroading in our state's history. Under the trestle are the Rivers of Tennessee Fountains, 31 vertical water fountains representing the predominant waterways in Tennessee. On each end of the riverwalk, you will find two clusters of Tennessee flags. Each cluster contains one large flag and eight smaller flags.

Along the park's east side, the Walkway of the Counties contains a time capsule from each of the 95 counties which are not to be opened until the Tricentennial in 2096. Commemorative granite bricks, purchased by citizens and engraved with their names, can be found along the Path of Volunteers, which extends down both sides of the park. The Court of 3 Stars, located at the northern end, is a focal point of the park made of red, white and blue granite. This area represents the three grand division of the state. It is also the site of the 95-bell Carillon which represents our musical heritage.

The World War II Memorial features an 18,000-pound granite globe floating on 1/8 inch of water. The countries on the globe are as they were during the war. The Civilian Conservation Corps Memorial, located at the park's north end, was dedicated in April 1998 by CCC Veterans and President Franklin Delano Roosevelt's grandson, David.

The 1,400-foot Wall of History, located on the west side of the park, is engraved with historic events that have occurred over the past two centuries. The center section of the park features a 2,000-seat amphitheater, composed of terraced lawns providing dramatic views of the State Capitol. The amphitheater will be the site of many events and ceremonies for visitors for years to come.

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GFOA CERTIFICATE OF ACHIEVEMENT

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Tennessee
Consolidated Retirement System

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2004

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



Nancy L. Ziehl

President

Jeffrey L. Esser

Executive Director

PUBLIC PENSION COORDINATING COUNCIL AWARD



**Public Pension Coordinating Council
Public Pension Standards
2005 Award**

Presented to

Tennessee Consolidated Retirement System

In recognition of meeting professional standards for
plan design and administration as
set forth in the Public Pension Standards.

Presented by the Public Pension Coordinating Council, a confederation of

National Association of State Retirement Administrators (NASRA)
National Conference on Public Employee Retirement Systems (NCPERS)
National Council on Teacher Retirement (NCTR)

A handwritten signature in cursive script that reads "Alan H. Winkle".

Alan H. Winkle
Program Administrator

INTRODUCTORY SECTION



CHAIRMAN OF THE BOARD'S LETTER

STATE OF TENNESSEE



TREASURY DEPARTMENT
STATE CAPITOL
NASHVILLE, TENNESSEE 37243

December 15, 2005

Dear Members of the Tennessee Consolidated Retirement System:

It is my pleasure to submit this annual financial report of the Tennessee Consolidated Retirement System. This is the eighteenth consecutive year that the financial report is being submitted to the Government Finance Officers Association for review. All previous reports have received the Certificate of Achievement for Excellence in Financial Reporting.

Administration: To better serve our members, the TCRS web site (located at www.treasury.state.tn.us/tcrs) includes a benefit calculation module, which allows members to input a limited amount of data to obtain a retirement benefit estimate. Further, TCRS forms and up-to-date information are available on-line to assist our members and participating employers. Information systems are continuing to be enhanced to allow for additional user-friendly access for members.

Investments: The return on TCRS investments during the fiscal year ended June 30, 2005 was 7.26%, slightly under the plan's assumed rate of return of 7.5%. The TCRS investment strategy has been somewhat conservative by favoring higher quality securities that mitigate some of the risks. A highly diversified portfolio is also used to minimize exposure to unpredictable events.

Financial Soundness of the Plan: Members of the retirement system should be assured that the benefits promised will be paid. TCRS is considered one of the strongest funded pension plans in the nation. TCRS has received an AAA long-term rating and an A-1(+) short-term rating by Standard and Poor's (S&P), the highest possible ratings issued by this nationally recognized rating agency. The actuarial valuation for July 1, 2003 offered significant challenges when considering the difficult investment environment we have experienced. Those challenges are expected to continue with the July 1, 2005 valuation.

The Legislature, the Board of Trustees and the TCRS staff have worked diligently to provide the best possible management of the system, to invest the system assets in a prudent manner without undue risk, to fund the system on an actuarially strong basis, and to provide the best possible services to the members in the system.

Sincerely,

A handwritten signature in cursive script that reads "Dale Sims".

Dale Sims, State Treasurer
Chairman of the Board

LETTER OF TRANSMITTAL

STATE OF TENNESSEE



TREASURY DEPARTMENT
TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
10TH FLOOR ANDREW JACKSON STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243

December 15, 2005

Board of Trustees
Tennessee Consolidated Retirement System
Nashville, TN 37243

Ladies and Gentlemen:

We are pleased to present to you the Tennessee Consolidated Retirement System (TCRS) comprehensive annual financial report for the fiscal year ended June 30, 2005. Responsibility for the accuracy of the data and the fairness and completeness of this presentation, including all disclosures, rests with the management of TCRS. To the best of our knowledge and belief, the enclosed data is accurate in all material respects and is reported in a manner designed to provide a precise representation of the financial position and results of operations of the system.

This report has been prepared in accordance with generally accepted accounting principles as promulgated or adopted by the Government Accounting Standards Board and the American Institute of Certified Public Accountants. Specific accounting treatments are detailed in the Notes to the Financial Statements found in the Financial Section of this report. Management is responsible for establishing and maintaining internal controls for TCRS. The accounting systems are designed to include internal controls to provide reasonable assurances regarding safekeeping of assets and the reliability of financial records. By statute, the Comptroller of the Treasury serves as the independent auditor for the system.

For additional discussion regarding financial information, please review Management's Discussion and Analysis located in the Financial Section of this report.

PROFILE OF TCRS

TCRS was established in 1972 with the consolidation of seven separate retirement systems for state employees, public higher education institution employees, public school teachers, and employees of political subdivisions electing to participate in TCRS. The state of Tennessee is responsible for the pension benefits of state employees and higher education employees, and funds a significant portion of the retirement liability for teachers through the Basic Education Program. Each of the 444 participating political subdivisions are responsible for the pension benefits of its employees. The TCRS is a qualified pension plan under Section 401(a) of the Internal Revenue Code. As such, the system is exempt from federal income taxation on its investment earnings. Since January 1, 1987, member contributions have been tax deferred under Section 414(h) of the Internal Revenue Code.

The TCRS was established as a retirement program for the public employees of Tennessee. A variety of services are provided for the membership including: investing assets; counseling of rights and benefits; publishing newsletters,

(continued)

**LETTER OF TRANSMITTAL
(CONTINUED)**

booklets, pamphlets, and financial statements; processing deductions for retiree insurance programs and federal income tax; calculating death, disability, and retirement benefits; and processing refund and prior service requests.

ECONOMIC CONDITION

Funding of TCRS is provided through employee and employer contributions plus earnings from the invested assets. A standard actuarial "advanced funding" method is used to provide for the accumulation of assets to fund the cost of retirement, disability, and death benefits provided by the system. The funding objective of TCRS is being met as the state and political subdivisions continue to make contributions to the plan at the rate established by the Board of Trustees. The Board is utilizing a strong actuarial method and has adopted reasonable actuarial assumptions for the determination of the appropriate employer contribution rates.

An actuarial valuation of TCRS is performed by an independent actuarial firm every two years to determine the funding requirements for the employers participating in TCRS. At July 1, 2003, the latest valuation date, the plan had an overall funding ratio of approximately 97%. The next actuarial valuation will be performed July 1, 2005 with the resulting employer contribution rates becoming effective July 1, 2006. The July 1, 2005 actuarial valuation will utilize the assumptions generated from the June 30, 2004 experience study.

Because TCRS is a strongly funded pension plan, volatility in investment income will cause employer contribution rates to fluctuate. Investment strategies have been adopted that somewhat reduce, but do not eliminate, this volatility. As part of this strategy, TCRS is in the final phase of absorbing investment losses accumulated several years ago. The resulting impact will increase employer contribution rates beginning July 1, 2006.

The investment market outlook continues to be flat creating significant challenges in meeting the 7.5% investment return assumed by TCRS. With the major market indices fluctuating within relatively narrow ranges, a premium will be placed on security selection.

AWARDS AND ACKNOWLEDGMENTS

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to Tennessee Consolidated Retirement System for its comprehensive annual financial report for the fiscal year ended June 30, 2004. This was the seventeenth consecutive year that the System has achieved this prestigious award.

The TCRS is a recipient of the Public Pension Principles Achievement Award. This program, administered by the Public Pension Coordinating Council, recognizes the professional achievements of public employee retirement systems.

The dedicated effort of the Treasury Department team to assemble the information contained in this publication is hereby acknowledged with our sincerest appreciation. The report will be provided to state legislators, members of the Board of Trustees, state officials, participating employers, and other interested parties.



Jill Bachus, TCRS Director



Thomas G. Milne, TCRS Chief Investment Officer

ADMINISTRATION AND MISSION

ADMINISTRATION

The State Treasurer is a constitutional officer elected every two years by a joint session of the General Assembly. He serves as the Chief Executive Officer of the Treasury Department, a part of the legislative branch of state government. The administration and operation of TCRS is one of the primary responsibilities of the State Treasurer. In order to meet the statutory requirements and fiduciary responsibilities of administering TCRS, the Treasurer appoints two executive officers: the Director of TCRS and the Chief Investment Officer.

The Director of TCRS is responsible for the daily operation of the retirement system which includes providing counseling services for the active and retired members; issuance of payments to retired members, disabled members, beneficiaries of deceased members, and refunds to terminated employees; enrollment of members; maintenance of member account balances and records; establishment of service credit; and issuance of various publications to inform members of their rights and benefits.

The Chief Investment Officer is responsible for the investment and oversight of TCRS assets in accordance with statutory guidelines and the investment policies and strategies established by the Board of Trustees.

Other divisions within the Treasury Department which support the operations of TCRS include Information Systems, Accounting, Management Services, Internal Audit and Personnel. Through these divisions, data processing services, accounting services, records maintenance, control reviews and personnel services are provided.

The administrative budget of TCRS is subject to approval by the General Assembly and is part of the overall annual budget process of the state of Tennessee. Funding for the operation of TCRS is provided by two sources. The state of Tennessee is responsible for the operation cost associated with state employees and higher education employees; the state and local education agencies share the cost related to K-12 teachers; political subdivisions are responsible for the operation cost associated with their employees.

MISSION

The mission of the Tennessee Consolidated Retirement System is to provide superior services to constituents in a cost-effective manner through qualified personnel while maintaining the highest ethical standards. The mission will be accomplished by TCRS in cooperation with the Board of Trustees, the Council on Pensions and Insurance, and the TCRS membership through the following objectives:

- ❖ *Exemplary Service* – To provide accurate, courteous and prompt service to members of TCRS.
- ❖ *Benefit Standards* – To provide retirement coverage through TCRS, social security and personal savings vehicles which will allow public employees to maintain their standard of living after retirement.
- ❖ *Funding Standards* – To provide for the long-term funding of TCRS on an actuarial basis which will ensure that sufficient assets will be accumulated to pay the statutory benefits of current and future retirees.
- ❖ *Staffing* – To attract and retain professional, highly-trained staff in an atmosphere conducive to innovation, challenges and a high level of performance.
- ❖ *Research* – To continuously perform studies on pension issues and to compare the TCRS plan with other public and private pension systems.
- ❖ *Management* – To manage by leading, planning, organizing and controlling the operation of TCRS in a cost-effective manner for the benefit of members and Tennessee taxpayers utilizing personnel, technology and capital efficiently, while providing the highest level of service.
- ❖ *Ethical Standards* – To maintain the highest ethical standards.
- ❖ *Investment Return* – To obtain the highest available return on investments consistent with the preservation of principal while maintaining sufficient liquidity to react to the changing environment and to pay benefits when due.

THE COUNCIL ON PENSIONS AND INSURANCE

THE COUNCIL ON PENSIONS AND INSURANCE

Created as a legislative oversight committee, the Council on Pensions and Insurance develops, recommends, and establishes pension and retirement standards and maintains a progressive state policy on retirement. Additionally, the Council reviews legislation affecting state provided insurance programs for both active and retired members of the Tennessee Consolidated Retirement System.

The Council periodically reviews Tennessee’s retirement and state provided insurance provisions and recommends changes in state law as deemed necessary. Since its creation, the Council has continuously performed studies and comparisons of other pension systems including those of other states and private industry and the federal government’s social security program. All proposed legislation affecting Tennessee’s retirement laws must be reviewed by the Council before the legislature may take action. The Council is authorized to prepare and

propose amendments which are then forwarded to the standing committees to which the bills are referred. Information regarding the actuarial cost or impact of proposed legislation is provided by the Council to the other members of the legislature. The staff of the TCRS director also serves as staff to the Council.

The voting membership of the Council consists of the Speaker of each house of the General Assembly; the officers of the House and the Senate Committees on Finance, Ways and Means; and three additional members of each finance committee. The Speaker of the Senate may designate a member of the Senate and the Speaker of the House of Representatives may designate a member of the House to serve as alternates to vote or otherwise act at Council meetings in absence of the respective speaker. Nonvoting members include the Commissioner of Personnel, the Commissioner of Finance and Administration, the Comptroller of the Treasury, the State Treasurer, and the Director of TCRS.

VOTING MEMBERS - SENATORS



Tim Burchett



Jerry Cooper



Douglas Henry
*Finance, Ways
& Means Chair*



James Kyle



Randy McNally
*Finance, Ways &
Means Vice-Chair*



John S. Wilder
Lieutenant Governor

(continued)

**THE COUNCIL ON PENSIONS AND INSURANCE
(CONTINUED)**

VOTING MEMBERS – REPRESENTATIVES



Stratton Bone



Tommie Brown



Craig Fitzhugh
*Council Chair
Finance, Ways &
Means Chair*



Steve McDaniel



Jimmy Naifeh
Speaker of the House



Johnny Shaw
*Finance, Ways &
Means Secretary*



Harry Tindell
*Finance, Ways &
Means Vice Chair*

NON-VOTING MEMBERS



Jill Bachus
TCRS Director



Randy Camp
Commissioner of Personnel



Dave Goetz
*Commissioner of Finance
& Administration*



John Morgan
Comptroller of the Treasury



Dale Sims
State Treasurer

THE BOARD OF TRUSTEES

THE BOARD OF TRUSTEES

The Tennessee Consolidated Retirement System Board of Trustees is responsible for the general administration and proper operation of TCRS within the requirements and provisions of state statute (*T.C.A.*, Title 8, Chapters 34-37). The 19-member Board meets quarterly and is subject to the call of the chair for special meetings. Nine voting members constitute a quorum, and nine affirmative votes are needed for decision making.

The Board consists of nine ex-officio members, eight representatives of the active TCRS membership, and two representatives for retirees. Ex-officio members include the chair and vice-chair of the Legislative Council on Pensions and Insurance as nonvoting members, the Commissioner of Personnel, the Commissioner of Finance and Administration, the Comptroller of the Treasury, the Secretary of State, and the Administrative Director of the Courts. In addition, the State Treasurer sits as Chair of the Board, and the Director of TCRS serves as Secretary.

Employee representation consists of three teachers, one from each grand division of the state, two state employees from departments other than those represented by ex-officio members, and three representatives of local governments. The three teachers are elected for three-year terms by the Representative Assembly of the Tennessee Education Association; state employees elect two representatives who also serve three-year terms.

One representative is appointed for a two-year term by each of the following organizations: The Tennessee County Services Association, the Tennessee Municipal League and the Tennessee County Officials Association.

All employee representatives must be vested members of TCRS. The state retiree representative is appointed by the Governor. A retired teacher, selected by the Tennessee Retired Teachers Association, serves on the board in a non-voting capacity.

ELECTED MEMBERS



Michael Barker
*Tennessee Retired
Teacher Association*
Term Expires: June 30, 2006



Michael Fort
*Department of
Employment Security*
Term Expires: June 30, 2007



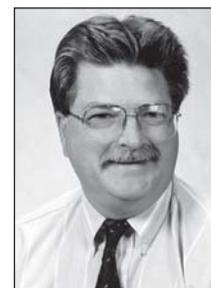
Rebecca Reel
East Tennessee Teacher
Term Expires: June 30, 2007



Timothy Trimble
West Tennessee Teacher
Term Expires: June 30, 2008



Judy Wahlstrom
*Department of
Children's Services*
Term Expires: June 30, 2007



Brian Randy Wright
Middle Tennessee Teacher
Term Expires: June 30, 2006

(continued)

THE BOARD OF TRUSTEES
(CONTINUED)

APPOINTED MEMBERS



Leonard Bradley
Retired Member
Term Expires: June 30, 2006



James Crumley
Tenn. Municipal League
Term Expires: June 30, 2007



Bill Kemp
Sumner County Clerk
Term Expires: June 30, 2007



David Seivers
Tenn. County Services Assoc.
Term Expires: June 30, 2007

EX-OFFICIO MEMBERS



Jill Bachus
TCRS Director



Randy Camp
Commissioner of Personnel



Cornelia Clark
*Administrative Director
of the Courts*



Riley Darnell
Secretary of State



Craig Fitzhugh
Council Chair



Dave Goetz
*Commissioner of Finance
& Administration*



Randy McNally
Council Vice-Chair



John Morgan
Comptroller of the Treasury



Dale Sims
State Treasurer

PROFESSIONAL CONSULTANTS**PROFESSIONAL CONSULTANTS**

Independent professional consultants are appointed by the Board of Trustees to advise the Board and the TCRS staff on investment, medical and actuarial issues. Service fees related to investment professionals may be found on page 50.

INVESTMENT ADVISORY COUNCIL

The Investment Advisory Council (IAC) was established to assist both the Board of Trustees and the TCRS investment staff. The investment professionals on the IAC serve five-year terms, meet quarterly and are available to the TCRS staff for consultation. IAC members include:

Frederick S. Crown, CFA
AmSouth Bank
Nashville, Tennessee

Henry Delicata
Vanderbilt University
Nashville, Tennessee

Susan Logan Huffman, CFA
Reliant Investment Management, LLC
Memphis, Tennessee

George B. Stadler, CFA
SunTrust Bank, Nashville
Nashville, Tennessee

Chuck Webb, CFA
Weaver C. Barksdale & Associates
Brentwood, Tennessee

INTERNATIONAL EQUITY INVESTMENT MANAGERS

The international investment managers are responsible for purchasing stock of companies domiciled in foreign countries as set out in the investment policy.

Marilyn Harrison
Walter Scott & Partners Ltd.
One Charlotte Square
Edinburgh EH2 4DZ
Scotland

Lofton Holder
J.P. Morgan Investment Management
522 Fifth Avenue
New York, New York 10036

John Lowman
SG Asset Management (Singapore)
c/o Trust Co. of the West
200 Park Avenue, 22nd Fl.
New York, New York 10166

Alec McAuley
Putnam Investments
One Post Office Square
Boston, Massachusetts 02109

Neil Ostrer
Marathon Asset Management
Orion House
5 Upper St. Martin's Lane
London WC2H 9EA
England

GENERAL INVESTMENT CONSULTANT

An investment consultant is employed to assist in the long-term financial planning process, to evaluate various investment strategies, to measure investment performance, to determine whether the system's objectives are being met, to research investment proposals regarding the use of new asset classes or variations of existing asset classes and to provide investment information on various issues which may arise.

Pete Keliuotis
Strategic Investment Solutions, Inc.
333 Bush Street
Suite 2000
San Francisco, CA 94104

(continued)

**PROFESSIONAL CONSULTANTS
(CONTINUED)**

REAL ESTATE INVESTMENT CONSULTANT

The real estate consultant provides general market advice relative to real estate, measures performance of real estate properties, assists in the formulation of policy and assists in the selection of real estate advisors.

Frank L. Blaschka
The Townsend Group
Skylight Office Tower
1660 West Second Street
Suite 450
Cleveland, Ohio 44113

REAL ESTATE INVESTMENT ADVISORS

The real estate investment advisors identify potential co-investors as well as prospective real estate transactions.

Joseph Azelby
J.P. Morgan Fleming Asset Management, Inc.
522 Fifth Avenue, 9th Floor
New York, New York 10036

Alan Connor
Cornerstone Real Estate Advisers LLC
One Financial Plaza, Suite 1700
Hartford, Connecticut 06103

Stephen J. Furnary
Clarion Partners
335 Madison Avenue
New York, New York 10017

Michael A. Ruane
TA Associates Realty
28 State Street, 10th Floor
Boston, Massachusetts 02109

Randall C. Mundt, President & CIO
Principal Global Investors
801 Grand Avenue
Des Moines, Iowa 50392

MASTER CUSTODIAN BANK

The Master Custodian bank settles all financial investment transactions and provides custody services for TCRS assets.

John P. Roth
The Bank of New York
1 Wall Street
New York, New York 10286

THE MEDICAL BOARD

The physicians serving on the Medical Board evaluate applications for disability retirement to determine whether the applicants are totally and permanently disabled and unable to engage in gainful employment. Additionally, the panel reviews medical data submitted by disabled retirees who are subject to periodic evaluation. The Medical Board consists of the following:

Suzanne Fletcher, M.D.
Brentwood, Tennessee

Barry R. Siegel, M.D.
Memphis, Tennessee

Jeffrey Summers, M.D.
Knoxville, Tennessee

CONSULTING ACTUARY

An independent consulting actuarial firm performs an actuarial valuation every two years to determine the funding status of the system and recommend employer contribution rates. The actuary also conducts an experience study every four years to evaluate and adjust actuarial assumptions and methods.

Justin Thacker
Bryan, Pendleton, Swats & McAllister, LLC
5301 Virginia Way
Suite 400
Brentwood, Tennessee 37027

OTHER PROFESSIONAL SERVICES

State statute provides that the state Attorney General and Reporter will be the legal advisor of the Board and that the Office of the Comptroller of the Treasury will conduct an annual audit of the TCRS. These government officers are as follows:

Paul G. Summers
Attorney General/Reporter
Nashville, Tennessee

John G. Morgan
Comptroller of the Treasury
Nashville, Tennessee

TREASURY DEPARTMENT EXECUTIVE STAFF**TREASURER'S OFFICE**

Treasurer	Dale Sims	(615) 741-2956
Executive Assistant	Janice H. Cunningham	(615) 741-2956
Assistant to the Treasurer	Steven Curry, CPA-inactive, CEBS, CCM	(615) 532-8045
Staff Assistant to the Treasurer	Nathan Burton	(615) 741-2956
Human Resource Director	Ann Taylor-Tharpe	(615) 741-2956

TCRS INVESTMENTS

Assistant to the Treasurer	Ed Hennessee, CFP	(615) 532-1167
Chief Investment Officer	Thomas Milne, CFA	(615) 532-1157
Equity Director	Michael Keeler, CFA	(615) 532-1165
Senior Equity Portfolio Manager	Jeremy Conlin, CLU, ChFC, CFA	(615) 532-1152
Senior Equity Portfolio Manager	Jim Robinson, CFA	(615) 532-1177
Senior Equity Portfolio Manager	Roy Wellington, CFA	(615) 532-1151
Senior Fixed Income Portfolio Manager	Terry Davis, CFA	(615) 253-5416
Real Estate Director	Peter Katseff	(615) 532-1160
Senior Short-Term Portfolio Manager	Randy Graves, CPA-inactive	(615) 532-1154
Cash Management and Short-Term Portfolio Manager	Tim McClure, CCM	(615) 532-1166

RETIREMENT ADMINISTRATION

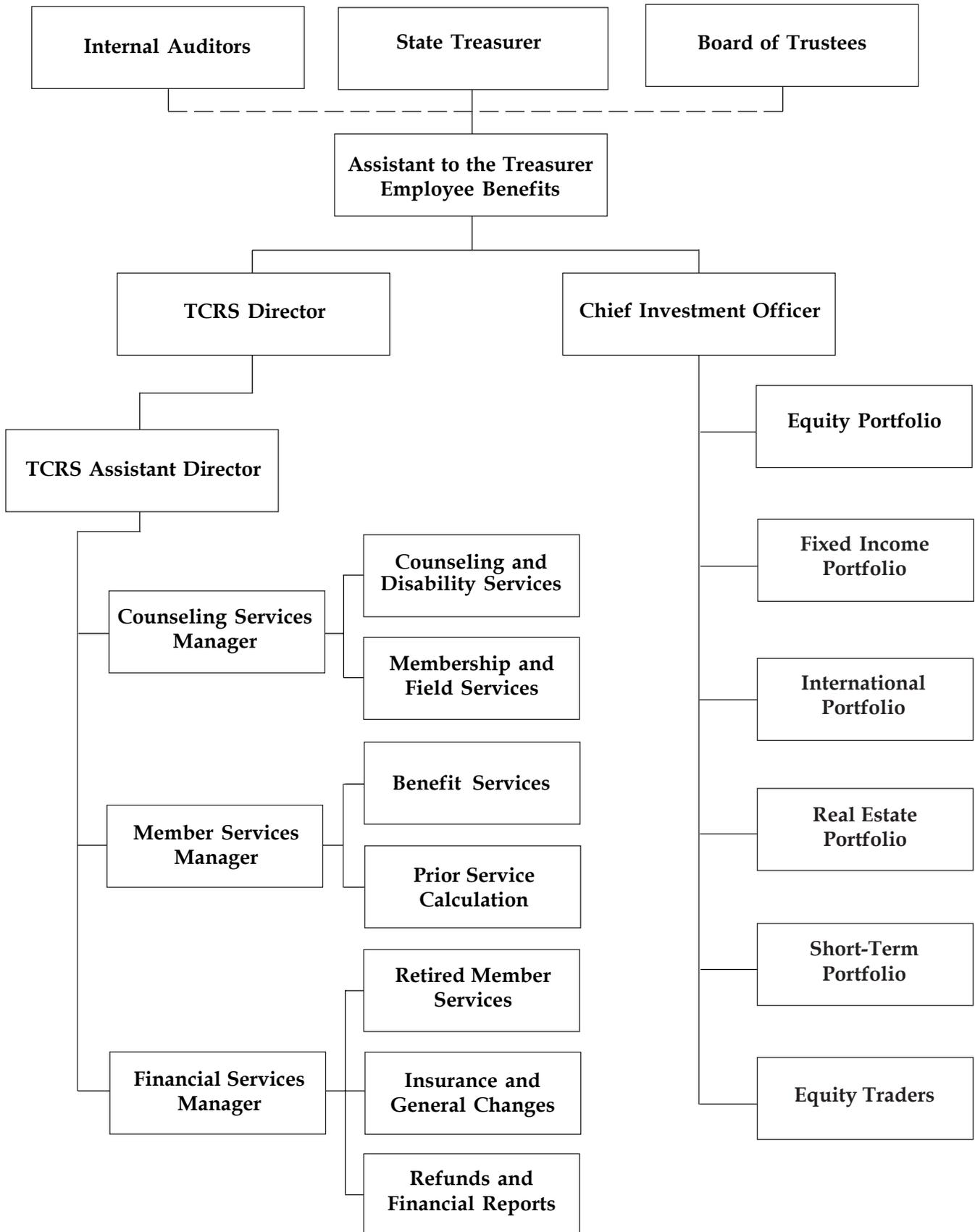
TCRS Director	Jill Bachus, CPA	(615) 741-7063
TCRS Assistant Director	Velva Booker	(615) 741-7063
TCRS Director of Deferred Compensation	Beth Chapman, CPA	(615) 741-7063
Publications Editor/Web Developer	Rick Mullins	(615) 741-7063
Publications Officer	Shirley Chatman	(615) 741-7063
General Counsel	Mary Roberts-Krause, JD	(615) 741-7063
Counsel	Vernon G. Bush, JD	(615) 741-7063
Director of Old Age and Survivors Insurance	Mary E. Smith	(615) 741-7902
Counseling Services Manager	Donna Finley	(615) 741-1971
Member Services Manager	Fred Marshall, CPA	(615) 741-1971
Financial Services Manager	Jamie Wayman, CPA	(615) 741-4913

OTHER DIVISIONS

Assistant to the Treasurer	Rick DuBray, CPA	(615) 253-5764
Director of Accounting	Kim Morrow, CPA	(615) 532-3840
Assistant Director of Accounting	Connie Gibson, CPA	(615) 532-8051
Director of Fiscal Services	Brian Derrick, CPA	(615) 532-8552
Assistant to the Treasurer	Newton Molloy III, CDP	(615) 532-8035
Director of Computer Operations	Sam Baker, CCP, CDP	(615) 532-8026
Director of Internal Audit	Britt Wood, CPA	(615) 253-2018
Director of Risk Management	Steve Gregory	(615) 741-1009
Manager of Treasury Operations	Gaylon Bandy	(615) 741-8202
Director of Unclaimed Property	John Gabriel	(615) 253-5354
Director of Claims Administration	Anne Adams	(615) 741-9957
Manager of Criminal Injury Claims	Amy Dunlap	(615) 741-9962
East Tennessee Claims Commissioner	Vance Cheek, Jr., JD	(423) 854-5330
Middle Tennessee Claims Commissioner	Stephanie Reeves, JD	(615) 253-1626
West Tennessee Claims Commissioner	Nancy Miller-Herron, JD	(731) 364-2440
Administrative Clerk, Claims Commission	Marsha Richeson	(615) 532-5385

*The Treasurer is housed on the 1st floor of the State Capitol Building.
Divisions are housed on the 9th, 10th, and 11th floors of the Andrew Jackson Building*

ORGANIZATION CHART



FINANCIAL SECTION



photo by Jed DeKalb

INDEPENDENT AUDITOR'S REPORT



STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF STATE AUDIT

SUITE 1500
JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-0264
PHONE (615) 401-7897
FAX (615) 532-2765

Independent Auditor's Report

December 15, 2005

The Honorable John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Morgan:

We have audited the accompanying statements of plan net assets of the Tennessee Consolidated Retirement System as of June 30, 2005, and June 30, 2004, and the related statements of changes in plan net assets for the years then ended. These financial statements are the responsibility of the Tennessee Consolidated Retirement System's management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the board of trustees of the Tennessee Consolidated Retirement System; approving accounting policies of the state as prepared by the state's Department of Finance and Administration; approving certain state contracts; and participating in the negotiation and procurement of services for the state.

As discussed in Note A.1., the financial statements present only the Tennessee Consolidated Retirement System, pension trust funds of the State of Tennessee, and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2005, and June 30, 2004, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

(continued)

**INDEPENDENT AUDITOR'S REPORT
(CONTINUED)**

The Honorable John G. Morgan
December 15, 2005
Page 2

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net assets of the Tennessee Consolidated Retirement System as of June 30, 2005, and June 30, 2004, and the changes in its plan net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

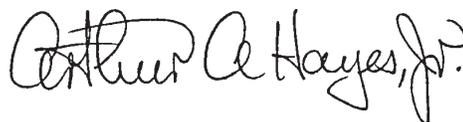
The management's discussion and analysis and the schedules of funding progress and employer contributions, as listed in the table of contents, are not required parts of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying financial information listed as supporting schedules in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

The introductory, investment, actuarial, and statistical sections, as listed in the table of contents, are presented for purposes of additional analysis and are not required parts of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 15, 2005, on our consideration of the Tennessee Consolidated Retirement System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Sincerely,



Arthur A. Hayes, Jr., CPA
Director

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEARS ENDED JUNE 30, 2005 & JUNE 30, 2004**

The Management of the Tennessee Consolidated Retirement System (TCRS) provides this discussion and analysis as an overview of the TCRS' financial activities for the fiscal years ended June 30, 2005 and June 30, 2004.

FINANCIAL HIGHLIGHTS

- ◆ The plan net assets (total assets minus total liabilities) of the TCRS at June 30, 2005 were \$27.2 billion, increasing over \$1.6 billion (6.4 percent) from the plan net assets at June 30, 2004. The net assets are held in trust to meet future benefit obligations.
- ◆ The TCRS relies upon contributions from employees and employers, along with investment income, to meet the funding requirements of an actuarially determined accrued liability. As of July 1, 2003, the date of the latest actuarial valuation, the TCRS' funded ratio was 99.8 percent for the SETHEEPP group and 91.9 percent for the PSPP group.
- ◆ Contribution revenue for fiscal year 2005 totaled \$844,856,748 - an increase of 37.1 percent compared to fiscal year 2004.
- ◆ Net investment income for fiscal year 2005 was \$1,850,367,215. During fiscal year 2005, the TCRS received an investment return on its portfolio of 7.3 percent, compared to 9.3 percent for fiscal year 2004.
- ◆ Total benefits and refunds paid for fiscal year 2005 were \$1,059,732,300 - an increase of 7.7 percent over fiscal year 2004 total benefits and refunds paid of \$984,377,076.
- ◆ Total administrative expenses for fiscal year 2005 were \$5,746,030 - an increase of 3.8 percent over fiscal year 2004 administrative expenses of \$5,534,441.

OVERVIEW OF THE FINANCIAL STATEMENTS

The TCRS financial statements consist of the Statement of Plan Net Assets (on pages 22 through 23), the Statement of Changes in Plan Net Assets (on pages 24 through 25), and the Notes to the Financial Statements (on pages 26 through 34). In addition, Required Supplementary Information is presented, which includes this Management's Discussion and Analysis, as well as the schedules and notes on pages 35 through 37.

The Statement of Plan Net Assets and the Statement of Changes in Plan Net Assets report information about the plan net assets (total assets in excess of total liabilities) as of the end of the fiscal year and the changes in those plan net assets during the fiscal year. These statements include all assets and liabilities using the accrual basis of accounting. Under the accrual basis of accounting, the current year's revenues and expenses are included in the financial activity, regardless of when cash is received or paid. The difference between the total assets and total liabilities on the Statement of Plan Net Assets, or net assets held in trust for pension benefits, provides a measurement of the financial position of the TCRS as of the end of the fiscal year. The Statement of Changes in Plan Net Assets provides information on the activities that caused the financial position to change during the fiscal year. Over time, increases or decreases in the plan net assets of the TCRS are one indicator of whether the system's financial health is improving or deteriorating.

In addition to the two basic financial statements, the reader should also review the Schedules of Funding Progress, the Schedules of Employer Contributions and the accompanying Notes to Required Supplementary Information to gain an understanding of the funded status of the TCRS over time. This information provides an indication of the TCRS' ability to meet both current and future benefit payment obligations. The Notes to the Financial Statements are also important to the reader's understanding of the financial statements and provide additional information regarding the TCRS, such as descriptions of the plans administered by the TCRS, including contribution and benefit provisions, and information about the accounting policies and investment activities.

(continued)

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEARS ENDED JUNE 30, 2005 & JUNE 30, 2004 (CONTINUED)

ANALYSIS OF ASSETS, LIABILITIES AND PLAN NET ASSETS

At June 30, 2005, the TCRS had plan net assets (total assets in excess of total liabilities) of \$27.2 billion, an increase of over \$1.6 billion (6.4 percent) from \$25.6 billion at June 30, 2004. The assets of the TCRS consist primarily of investments. During fiscal year 2005, all portfolios realized positive returns, thus contributing to \$1.85 billion in net investment income. Condensed financial information comparing the TCRS' plan net assets for the past three fiscal years is below.

PLAN NET ASSETS

			FY05 - FY04		FY04 - FY03	
			Percentage		Percentage	
	June 30, 2005	June 30, 2004	Change	June 30, 2003	Change	
ASSETS						
Cash and cash equivalents	\$ 804,694,718	\$ 1,287,694,472	(37.5) %	\$ 1,717,734,541	(25.0) %	
Contributions receivable	59,611,297	52,655,042	13.2 %	46,850,736	12.4 %	
Investment income						
receivables	168,791,063	136,353,991	23.8 %	134,284,002	1.5 %	
Investments sold	28,751,524	84,576,463	(66.0) %	59,060,030	43.2 %	
Foreign currency receivable	177,749,703	46,030,024	286.2 %	523,209,732	(91.2) %	
Short-term securities	231,988,352	564,645,773	(58.9) %	498,577,125	13.3 %	
Long-term investments	25,968,351,692	23,486,279,358	10.6 %	21,736,948,082	8.0 %	
TOTAL ASSETS	<u>27,439,938,349</u>	<u>25,658,235,123</u>	6.9 %	<u>24,716,664,248</u>	3.8 %	
LIABILITIES						
Death benefits, refunds and						
other payables	6,721,778	2,350,420	186.0 %	1,244,060	88.9 %	
Investments purchased	41,541,888	20,722,128	100.5 %	387,262,530	(94.6) %	
Other investment payables	2,295,936	2,127,641	7.9 %	2,154,173	(1.2) %	
Foreign currency payable	173,116,862	46,518,682	272.1 %	547,519,127	(91.5) %	
TOTAL LIABILITIES	<u>223,676,464</u>	<u>71,718,871</u>	211.9 %	<u>938,179,890</u>	(92.4) %	
NET ASSETS HELD IN TRUST						
FOR PENSION BENEFITS	<u>\$ 27,216,261,885</u>	<u>\$ 25,586,516,252</u>	6.4 %	<u>\$ 23,778,484,358</u>	7.6 %	

ANALYSIS OF REVENUES AND EXPENSES

An increase in employer contribution rates adopted pursuant to the actuarial valuation performed as of July 1, 2003 and effective for fiscal year 2005, resulted in contributions for fiscal year 2005 increasing by \$228.8 million (37.1 percent) over contributions for fiscal year 2004. Although employer contribution rates did not change between fiscal year 2004 and 2003, the increase of \$20 million (3.4 percent) for these years is attributed to increased salaries. As mentioned in the Analysis of Assets, Liabilities and Plan Net Assets section above, the continued market progress contributed to positive net investment income. Net investment income for the year ended June 30, 2005 totaled \$1,850,367,215, a decrease of \$331 million versus fiscal year 2004. Net investment income for the year ended June 30, 2004 totaled \$2,181,853,628, an increase of \$1.1 billion versus fiscal year 2003. Market conditions have resulted in a return to the TCRS portfolio of 7.3 percent during fiscal year 2005 and 9.3 percent during fiscal year 2004.

Total benefits and refunds paid during the year ended June 30, 2005 were \$1,059,732,300, an increase of 7.7 percent over fiscal year 2004 total benefits and refunds paid. Total refunds and benefits paid during the year ended June 30,

(continued)

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEARS ENDED JUNE 30, 2005 & JUNE 30, 2004 (CONTINUED)**

2004 of \$984,377,076 increased 8.4 percent over fiscal year 2003 total benefits and refunds paid. The increase in benefit expenses can be attributed to 1.9 percent and 2.4 percent cost of living adjustments awarded to retirees on July 1, 2004 and July 1, 2003, respectively. In addition, more retirees were added to payroll than removed during these fiscal years.

In addition, administrative expenses for the year ended June 30, 2005 were \$5,746,030, an increase of 3.8 percent over fiscal year 2004 administrative expenses. Administrative expenses for fiscal year 2004 of \$5,534,441 increased 9.5 percent over administrative expenses for fiscal year 2003.

Condensed financial information comparing the TCRS' revenues and expenses for the past three fiscal years follows.

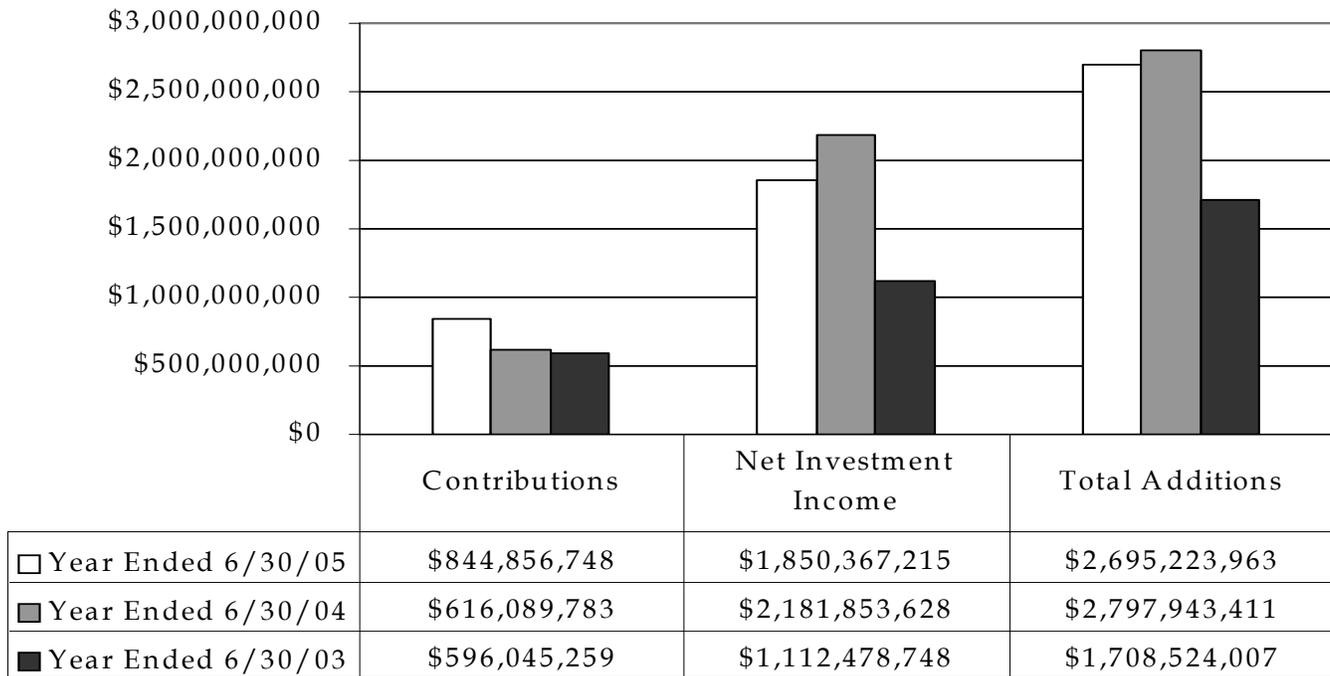
CHANGES IN PLAN NET ASSETS

	For the Year Ended June 30, 2005	For the Year Ended June 30, 2004	FY05 - FY04 Percentage Change	For the Year Ended June 30, 2003	FY04 - FY03 Percentage Change
ADDITIONS					
Contributions	\$ 844,856,748	\$ 616,089,783	37.1 %	\$ 596,045,259	3.4 %
Investment income					
Net appreciation (depreciation) in fair value of investments	938,346,880	1,310,811,851	(28.4) %	268,965,778	387.4 %
Interest, dividends and other investment income	927,714,221	885,509,528	4.8 %	857,325,990	3.3 %
Less: Investment expense	(15,693,886)	(14,467,751)	8.5 %	(13,813,020)	4.7 %
Net investment income	1,850,367,215	2,181,853,628	(15.2) %	1,112,478,748	96.1 %
TOTAL ADDITIONS	<u>2,695,223,963</u>	<u>2,797,943,411</u>	(3.7) %	<u>1,708,524,007</u>	63.8 %
DEDUCTIONS					
Annuity benefits					
Retirement benefits	775,283,016	716,339,066	8.2 %	662,075,122	8.2 %
Survivor benefits	50,388,267	46,416,539	8.6 %	42,638,112	8.9 %
Disability benefits	24,626,014	23,590,867	4.4 %	21,781,588	8.3 %
Cost of living	173,707,939	163,627,253	6.2 %	150,690,914	8.6 %
Death benefits	4,911,365	4,477,589	9.7 %	4,046,275	10.7 %
Refunds	30,815,699	29,925,762	3.0 %	26,631,386	12.4 %
Administrative expenses	5,746,030	5,534,441	3.8 %	5,055,824	9.5 %
TOTAL DEDUCTIONS	<u>1,065,478,330</u>	<u>989,911,517</u>	7.6 %	<u>912,919,221</u>	8.4 %
NET (DECREASE) INCREASE	1,629,745,633	1,808,031,894	(9.9) %	795,604,786	127.3 %
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS					
BEGINNING OF YEAR	25,586,516,252	23,778,484,358	7.6 %	22,982,879,572	3.5 %
END OF YEAR	<u>\$ 27,216,261,885</u>	<u>\$ 25,586,516,252</u>	6.4 %	<u>\$ 23,778,484,358</u>	7.6 %

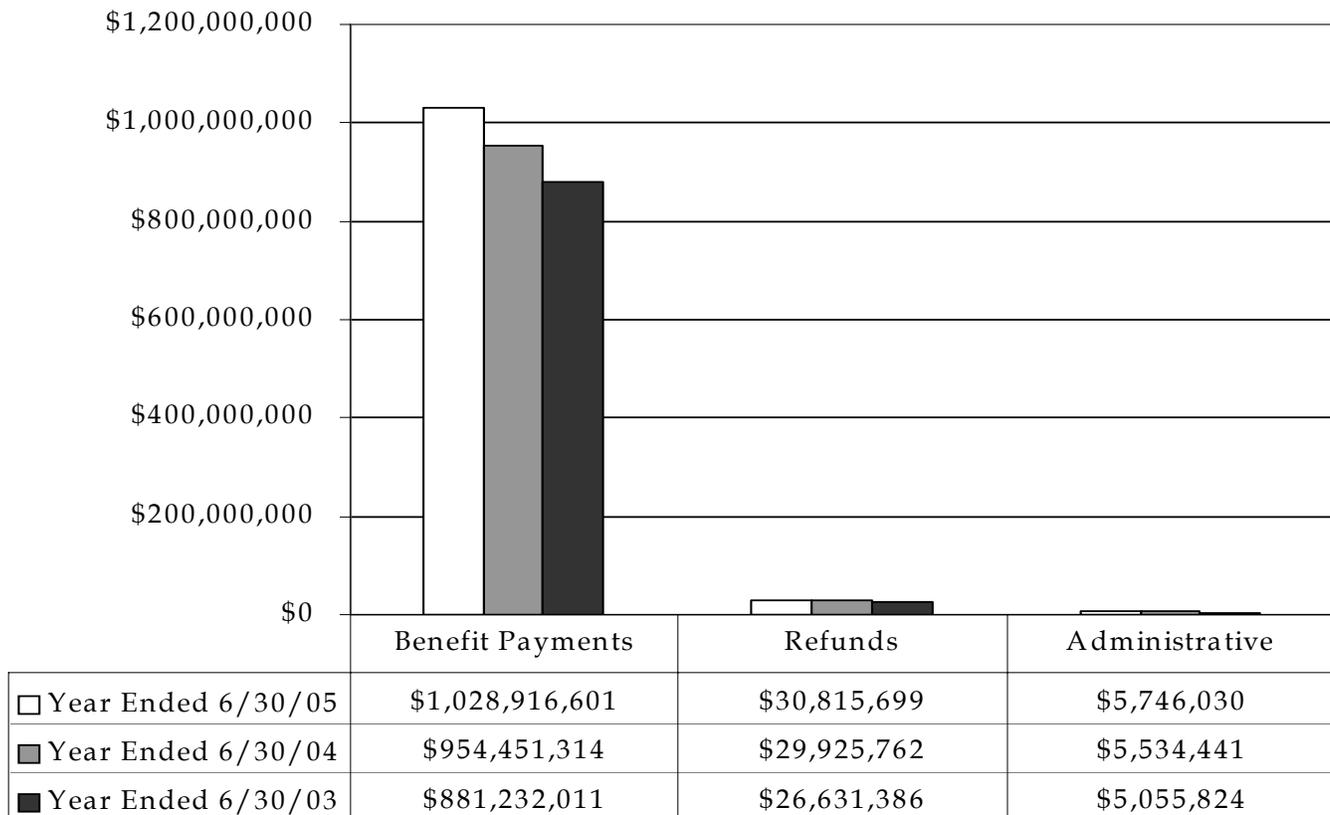
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**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEARS ENDED JUNE 30, 2005 & JUNE 30, 2004 (CONTINUED)**

REVENUES BY TYPE



EXPENSES BY TYPE



(continued)

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEARS ENDED JUNE 30, 2005 & JUNE 30, 2004 (CONTINUED)**

ECONOMIC FACTORS, FUTURE FUNDING PROVISIONS, OVERALL OUTLOOK

There was continued strength in both the domestic and international stock markets for the year ended June 30, 2005. The S&P 1500 index, TCRS' domestic equity benchmark, had a return of 7.24% for the fiscal year ended June 30, 2005, preceded by a double-digit return of 19.11% for fiscal year 2004. The international equity market, as represented by the EAFE index, rebounded nicely for the year ended June 30, 2004 with a 32.37% return, followed by a 14.13% return in fiscal year 2005. The domestic bond market, as measured by the Lehman Aggregate index, had an annual return of only .32% at June 30, 2004, which rebounded with a 6.8% return during fiscal year 2005. The international bond market return of 7.62% and real estate at 18.02% represents positive market returns.

In 2004, a strong stock market balanced an under-performing bond market. Broad market strength was realized during 2005, although several indices have not yet fully recovered from the weak markets during the 2000-2003 period.

The employer contribution rate increased July 1, 2004 for most of the employers participating in TCRS. The increase was the result of the July 1, 2003 actuarial valuation that took into consideration that investment results were less than the earnings assumptions for the two years since the last actuarial valuation. With the asset smoothing method utilized for valuation purposes that recognized only a portion of the underperformance of investment income, upward pressure on the employer rate is expected for the next actuarial valuation to be performed effective July 1, 2005. However, some upward pressure will be mitigated by the positive return of 9.32% realized for the year ended June 30, 2004. It was refreshing to realize such a return after three straight years where returns were less than the actuarial assumption of 7.5%. With TCRS being such a strongly funded plan, volatility in investment income will cause employer contribution rates to fluctuate.

CONTACTING THE TCRS

This report is designed to provide a financial overview of the TCRS to state legislators, members of the Board of Trustees of the TCRS, state officials, participating employers and any other interested parties. Questions or requests for additional information regarding the financial information presented in this report may be addressed in writing to the Tennessee Treasury Department, Consolidated Retirement System, 10th Floor Andrew Jackson Building, Nashville, TN 37243-0230.

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
COMPARATIVE STATEMENTS OF PLAN NET ASSETS
AS OF JUNE 30, 2005 AND JUNE 30, 2004

	State Employees, Teachers, Higher Education Employees Pension Plan (SETHEEPP)	Political Subdivisions Pension Plan (PSPP)
ASSETS		
Cash and cash equivalents	<u>\$ 685,337</u>	<u>\$ 119,358</u>
Receivables		
Member contributions receivable	15,057	3,750
Employer contributions receivable	28,637	12,167
Accrued interest receivable	123,300	21,474
Accrued dividends receivable	19,264	3,355
Real estate income receivable	1,191	207
Foreign currency receivable	151,385	26,365
Investments sold	24,487	4,265
Total receivables	<u>363,321</u>	<u>71,583</u>
Investments, at fair value		
Short-term securities	197,578	34,410
Government securities	9,953,162	1,733,442
Corporate securities	2,147,044	373,929
Corporate stocks	9,603,998	1,672,632
Real estate	412,332	71,812
Total investments	<u>22,314,114</u>	<u>3,886,225</u>
TOTAL ASSETS	<u>23,362,772</u>	<u>4,077,166</u>
LIABILITIES		
Accounts payable		
Death benefits and refunds payable	928	1,880
Other	3,913	0
Investments purchased	35,380	6,162
Foreign currency payable	147,439	25,678
Other investment payables	1,956	340
TOTAL LIABILITIES	<u>189,616</u>	<u>34,060</u>
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS (Schedules of funding progress for the plan are presented on page 35.)	<u>\$ 23,173,156</u>	<u>\$ 4,043,106</u>

See accompanying Notes to the Financial Statements

(continued)

(CONTINUED)

June 30, 2005 Total	State Employees, Teachers, Higher Education Employees Pension Plan (SETHEEPP)	Political Subdivisions Pension Plan (PSPP)	June 30, 2004 Total
<u>\$ 804,695</u>	<u>\$ 1,102,224</u>	<u>\$ 185,470</u>	<u>\$ 1,287,694</u>
18,807	17,687	3,954	21,641
40,804	19,905	11,109	31,014
144,774	100,996	16,995	117,991
22,619	15,719	2,644	18,363
1,398	0	0	0
177,750	39,400	6,630	46,030
28,752	72,395	12,182	84,577
<u>434,904</u>	<u>266,102</u>	<u>53,514</u>	<u>319,616</u>
231,988	483,319	81,327	564,646
11,686,604	9,311,372	1,566,810	10,878,182
2,520,973	1,597,428	268,796	1,866,224
11,276,630	8,798,054	1,480,436	10,278,490
484,144	396,641	66,742	463,383
<u>26,200,339</u>	<u>20,586,814</u>	<u>3,464,111</u>	<u>24,050,925</u>
<u>27,439,938</u>	<u>21,955,140</u>	<u>3,703,095</u>	<u>25,658,235</u>
2,808	1,038	1,267	2,305
3,913	45	0	45
41,542	17,737	2,985	20,722
173,117	39,819	6,700	46,519
2,296	1,821	307	2,128
<u>223,676</u>	<u>60,460</u>	<u>11,259</u>	<u>71,719</u>
<u>\$ 27,216,262</u>	<u>\$ 21,894,680</u>	<u>\$ 3,691,836</u>	<u>\$ 25,586,516</u>

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
COMPARATIVE STATEMENTS OF CHANGES IN PLAN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2005 AND JUNE 30, 2004

	State Employees, Teachers, Higher Education Employees Pension Plan (SETHEEPP)	Political Subdivisions Pension Plan (PSPP)
ADDITIONS		
Contributions		
Member contributions	\$ 160,686	\$ 54,921
Employer contributions	448,154	181,096
Total contributions	<u>608,840</u>	<u>236,017</u>
Investment income		
Net appreciation in fair value of investments	800,850	137,497
Interest	547,898	94,067
Dividends	217,309	37,309
Real estate income, net of operating expenses	26,569	4,562
Total investment income	<u>1,592,626</u>	<u>273,435</u>
Less: Investment expense	<u>(13,394)</u>	<u>(2,300)</u>
Net investment income	<u>1,579,232</u>	<u>271,135</u>
TOTAL ADDITIONS	<u><u>2,188,072</u></u>	<u><u>507,152</u></u>
DEDUCTIONS		
Annuity benefits		
Retirement benefits	668,340	106,943
Survivor benefits	43,437	6,951
Disability benefits	21,229	3,397
Cost of living	154,522	19,186
Death benefits	3,731	1,180
Refunds	15,329	15,487
Administrative expense	3,008	2,738
TOTAL DEDUCTIONS	<u>909,596</u>	<u>155,882</u>
NET INCREASE	1,278,476	351,270
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS		
BEGINNING OF YEAR	<u>21,894,680</u>	<u>3,691,836</u>
END OF YEAR	<u><u>\$ 23,173,156</u></u>	<u><u>\$ 4,043,106</u></u>

See accompanying Notes to the Financial Statements

(continued)

(CONTINUED)

For the Year Ended June 30, 2005 Total	State Employees, Teachers, Higher Education Employees Pension Plan (SETHEEPP)	Political Subdivisions Pension Plan (PSPP)	For the Year Ended June 30, 2004 Total
\$ 215,607 629,250 <hr style="width: 100%;"/> 844,857	\$ 154,334 271,298 <hr style="width: 100%;"/> 425,632	\$ 50,650 139,808 <hr style="width: 100%;"/> 190,458	\$ 204,984 411,106 <hr style="width: 100%;"/> 616,090
938,347 641,965 254,618 31,131 <hr style="width: 100%;"/> 1,866,061 (15,694) <hr style="width: 100%;"/> 1,850,367 <hr style="width: 100%;"/> 2,695,224	1,124,041 579,747 157,233 22,357 <hr style="width: 100%;"/> 1,883,378 (12,406) <hr style="width: 100%;"/> 1,870,972 <hr style="width: 100%;"/> 2,296,604	186,771 96,331 26,126 3,715 <hr style="width: 100%;"/> 312,943 (2,062) <hr style="width: 100%;"/> 310,881 <hr style="width: 100%;"/> 501,339	1,310,812 676,078 183,359 26,072 <hr style="width: 100%;"/> 2,196,321 (14,468) <hr style="width: 100%;"/> 2,181,853 <hr style="width: 100%;"/> 2,797,943
775,283 50,388 24,626 173,708 4,911 30,816 5,746 <hr style="width: 100%;"/> 1,065,478 <hr style="width: 100%;"/> 1,629,746	617,659 40,022 20,341 145,767 3,149 15,305 2,935 <hr style="width: 100%;"/> 845,178 <hr style="width: 100%;"/> 1,451,426	98,680 6,394 3,250 17,860 1,329 14,621 2,599 <hr style="width: 100%;"/> 144,733 <hr style="width: 100%;"/> 356,606	716,339 46,416 23,591 163,627 4,478 29,926 5,534 <hr style="width: 100%;"/> 989,911 <hr style="width: 100%;"/> 1,808,032
25,586,516 <hr style="width: 100%;"/> \$ 27,216,262	20,443,254 <hr style="width: 100%;"/> \$ 21,894,680	3,335,230 <hr style="width: 100%;"/> \$ 3,691,836	23,778,484 <hr style="width: 100%;"/> \$ 25,586,516

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2005 AND JUNE 30, 2004

The Tennessee Consolidated Retirement System (TCRS) administers two defined benefit pension plans - State Employees, Teachers and Higher Education Employees Pension Plan (SETHEEPP) and Political Subdivisions Pension Plan (PSPP). Although the assets of the plans are commingled for investment purposes, each plan's assets may be used only for the payment of benefits to members of that plan, in accordance with the terms of the plan.

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. **Reporting Entity** - The TCRS is included in the State of Tennessee Financial Reporting Entity. Because of the state's fiduciary responsibility, the TCRS has been included as pension trust funds in the *Tennessee Comprehensive Annual Financial Report*.
2. **Measurement Focus and Basis of Accounting** - The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The financial statements have been prepared using the flow of economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Plan member contributions are recognized in the period of time for which the contributions are assessed. Plan employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each plan.

3. **Cash and Cash Equivalents** - Cash and cash equivalents by definition, includes cash and short-term investments with a maturity date within three months of the acquisition date. The state's accounting policy regarding the definition of cash and cash equivalents includes cash management pools as cash. Cash received by the TCRS that cannot be invested immediately in securities, or that is needed for operations, is invested in the State Pooled Investment Fund sponsored by the State of Tennessee and administered by the State Treasurer. The classification of cash and cash equivalents also includes cash invested in a short-term, open-end mutual fund under the contractual arrangement for master custody services.
4. **Method Used to Value Investments** - Investments are reported at fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. The fair value of real estate investments is determined at least every three years by qualified independent appraisers who are members of the Appraisal Institute and internally by real estate advisors for those years when independent appraisals are not performed. Investment income consists of realized and unrealized appreciation (depreciation) in the fair value of investments. Interest income is recognized when earned. Securities and securities transactions are recorded in the financial statements on trade-date basis.
5. **Receivables** - Receivables primarily consist of interest, which is recorded when earned. The receivables for contributions as of June 30, 2005 consist of member contributions of \$15 million and \$3.7 million due to SETHEEPP and PSPP respectively, and employer contributions of \$28.6 million and \$12.2 million due to SETHEEPP and PSPP respectively. The receivables for contributions as of June 30, 2004 consist of member contributions of \$17.7 million and \$3.9 million due to SETHEEPP and PSPP respectively, and employer contributions of \$19.9 million and \$11.1 million due to SETHEEPP and PSPP respectively.
6. **Adoption of New Accounting Pronouncement** - During the year ended June 30, 2005, the TCRS adopted the provisions of Statement No. 40 of the Governmental Accounting Standards Board *Deposit and Investment Risk Disclosures - an amendment of GASB Statement No. 3*. The adoption of this statement requires the TCRS to provide certain additional disclosures, as well as modify other disclosures relating to investment and deposit risks, including credit risk, custodial credit risk, concentrations of credit risk, interest rate risk and foreign currency risk. Disclosure information relative to the year ended June 30, 2004 has been restated to conform to the new pronouncement.

(continued)

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2005 AND JUNE 30, 2004 (CONTINUED)

7. **Reclassifications** - Certain investment amounts previously presented on the June 30, 2004 Statement of Plan Net Assets have been reclassified for comparative purposes. Corporate bonds in the amount of \$20,009,658 have been reclassified as government bonds. Government bonds in the amount of \$9,803,600 have been reclassified as corporate bonds, and corporate bonds in the amount of \$1,767,564 have been reclassified as corporate stocks.

B. PLAN DESCRIPTIONS AND CONTRIBUTION INFORMATION

At July 1, 2003, the date of the latest actuarial valuation, the membership of each plan consisted of the following:

	SETHEEPP	PSPP
Retirees and beneficiaries currently receiving benefits	59,959	23,162
Terminated members entitled to but not receiving benefits	16,721	3,972
Current active members	<u>127,597</u>	<u>71,320</u>
Total	204,277	98,454
Number of participating employers	140	418

State Employees, Teachers and Higher Education Employees Pension Plan

Plan Description - SETHEEPP is a cost-sharing, multiple employer defined benefit pension plan that covers the employees of the state, teachers with Local Education Agencies (LEA's) and higher education employees. The TCRS provides retirement benefits as well as death and disability benefits to plan members and their beneficiaries. Benefits are determined by a formula using the member's high five-year average salary and years of service. Members become eligible to retire at the age of 60 with five years of service or at any age with 30 years of service. A reduced retirement benefit is available to vested members who are at least 55 years of age or have 25 years of service. Disability benefits are available to active members with five years of service who become disabled and cannot engage in gainful employment. There is no service requirement for disability that is the result of an accident or injury occurring while the member was in the performance of duty. Members joining the plan on or after July 1, 1979 are vested after five years of service. Members joining prior to July 1, 1979 are vested after four years of service. Compounded cost of living adjustments (COLA) are provided each July based on the percentage change in the Consumer Price Index (CPI) during the previous calendar year except that (a) no COLA is granted if the CPI is less than one-half percent; (b) a COLA of 1 percent will be granted if the CPI increases between one-half percent and one percent; (c) the maximum annual COLA is capped at three percent. Benefit provisions are established by state statute found in Title Eight, Chapters 34 through 37 of the *Tennessee Code Annotated*. State statutes are amended by the Tennessee General Assembly. Ad hoc increases may only be authorized by the General Assembly. Public safety officers receive an additional supplemental benefit that is paid from age 60 to age 62.

Superseded Systems and Certain Employment Classifications - Members of superseded systems that became members of the TCRS at consolidation in 1972, have their rights preserved to the benefits of the superseded system, if the benefit from the superseded plan exceeds that provided by the Group 1 (teachers and general employees) TCRS formula. Likewise, public safety employees and officials of TCRS Groups 2, 3 and 4 are entitled to the benefits of those formulas, if better than the Group 1 benefits.

Contributions and Reserves - Effective July 1, 1981, the plan became noncontributory for most state and higher education employees. The contribution rate for teachers is five percent of gross salary. The employers contribute a set percentage of their payrolls, determined by an actuarial valuation. *Tennessee Code Annotated* Title Eight, Chapter 37 provides that the contribution rates be established and may be amended by the Board of Trustees of the TCRS. The administrative budget for the plan is approved through the state of Tennessee's annual budget process. Funding for the administrative budget is included in employer contributions.

The net assets of the plan are legally required to be reserved in two accounts, the Member Reserve and the Employer Reserve. The Member Reserve represents the accumulation of employee contributions plus interest.

(continued)

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2005 AND JUNE 30, 2004 (CONTINUED)

The Employer Reserve represents the accumulation of employer contributions, investment income and transfers from the Member Reserve for retiring members. Benefit payments and interest credited to the members' accounts are reductions to the Employer Reserve. At June 30, 2005, the plan's Member Reserve and Employer Reserve were fully funded with balances of \$3,167.8 million and \$20,005.3 million, respectively. At June 30, 2004, the plan's Member Reserve and Employer Reserve were fully funded with balances of \$3,059.2 million and \$18,835.5 million, respectively.

Political Subdivisions Pension Plan

Plan Description - PSPP is an agent multiple-employer defined benefit pension plan that covers the employees of participating political subdivisions of the state of Tennessee. Employee class differentiations are not made under PSPP. The TCRS provides retirement benefits as well as death and disability benefits to plan members and their beneficiaries. Benefits are determined by a formula using the member's high five-year average salary and years of service. Members become eligible to retire at the age of 60 with five years of service or at any age with 30 years of service. A reduced retirement benefit is available to vested members who are at least 55 years of age or have 25 years of service. Disability benefits are available to active members with five years of service who become disabled and cannot engage in gainful employment. There is no service requirement for disability that is the result of an accident or injury occurring while the member was in the performance of duty. Members joining the plan prior to July 1, 1979 are vested after four years of service. Members joining on or after July 1, 1979 are vested upon completion of 10 years of service, unless five years vesting is authorized by resolution of the chief governing body. Cost of living adjustments (COLA) are the same as provided by SETHEEPP except that the local government may elect (a) to provide no COLA benefits or (b) to provide COLA benefits under a non-compounding basis rather than the compounded basis applicable under SETHEEPP. Benefit provisions are established and amended by state statute. Pursuant to Article Two, Section 24 of the *Constitution of the State of Tennessee*, the state cannot mandate costs on local governments. Any benefit improvement may be adopted by the governing body of a governmental entity participating in the TCRS.

Contributions and Reserves - Political subdivisions may elect contributory or noncontributory retirement for their employees. The contribution rate for contributory employees of political subdivisions is five percent of gross salary. The employers contribute a set percentage of their payrolls, equal to at least, the percentage determined by an actuarial valuation. State statute provides that the contribution rates be established and may be amended by the Board of Trustees of the TCRS. The administrative budget for the plan is approved through the state's annual budget process. Funding for the administrative budget is included in employer contributions.

The net assets of the plan are legally required to be reserved in two accounts, the Member Reserve and the Employer Reserve. The Member Reserve represents the accumulation of employee contributions plus interest. The Employer Reserve represents the accumulation of employer contributions, investment income and transfers from the Member Reserve for retiring members. Benefit payments and interest credited to the members' accounts are reductions to the Employer Reserve. At June 30, 2005, the plan's Member Reserve and Employer Reserve were fully funded with balances of \$795.4 million and \$3,247.7 million, respectively. At June 30, 2004, the plan's Member Reserve and Employer Reserve were fully funded with balances of \$746.9 million and \$2,944.9 million, respectively.

C. DEPOSITS AND INVESTMENTS

State statute authorizes the TCRS to maintain cash, not exceeding ten percent of the total amount of funds in the retirement system, on deposit in one or more banks, savings and loan associations or trust companies that are qualified as state depositories. The TCRS does not utilize its own bank accounts but invests in the State Pooled Investment Fund for the initial deposit of funds and for its operating cash needs. The State Pooled Investment Fund is authorized by state statute to invest funds in accordance with policy guidelines approved by the Funding Board of the State of Tennessee. The current resolution of that board gives the Treasurer authority to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers'

(continued)

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2005 AND JUNE 30, 2004 (CONTINUED)**

acceptances, certain repurchase agreements and various U.S. Treasury and Agency obligations. Prior to the adoption of the current investment policy on December 14, 2004, allowable investments also included obligations of the State of Tennessee pursuant to *Tennessee Code Annotated*, Section 9-4-602(b). The State Pooled Investment Fund is also authorized to enter into securities lending agreements in which U.S. Government Securities may be loaned for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities.

State statute also authorizes the TCRS to invest in bonds, debentures, preferred stock and common stock, real estate and in other good and solvent securities subject to the approval of the Board of Trustees, but further subject to the following statutory restrictions and provisions:

- a. The total sum invested in common and preferred stocks shall not exceed seventy-five percent (75 percent) of the total of the funds of the retirement system.
- b. The total sum invested in notes and bonds or other fixed income securities exceeding one year in maturity shall not exceed seventy-five percent (75 percent) of the total funds of the retirement system.
- c. Within the restrictions in (a) and (b) above, an amount not to exceed fifteen percent (15 percent) of the total of the funds of the retirement system may be invested in securities of the same kinds, classes, and investment grades as those otherwise eligible for investment in various approved foreign countries, provided that such percentage may be increased by the board with the subsequent approval of the council on pensions and insurance.
- d. Within the restrictions in (a) and (b) above, funds may be invested in Canadian securities which are substantially of the same kinds, classes and investment grades as those otherwise eligible for investment.
- e. The total amount of securities loaned under a securities lending program cannot exceed thirty percent (30 percent) of total assets.
- f. The total sum invested in real estate shall not exceed five percent (5 percent) of the market value of total assets.

State statute also authorizes the TCRS to invest in forward contracts to hedge its foreign currency exposure and to purchase or sell domestic stock index futures contracts for the purpose of asset allocation relating to the domestic equity portfolio. The total amount of the financial futures contract obligation shall not exceed five percent (5 percent) of the market value of total assets.

As of June 30, 2005 and June 30, 2004, the TCRS had the following investments:

(continued)

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2005 AND JUNE 30, 2004 (CONTINUED)

Investments
(Expressed in Thousands)

Investment Type	Fair Value as of 6/30/05	U.S. Treasury/ Agency (1)	Credit Quality Ratings					
			AAA	AA	A	BBB	A1 (2)	Not Rated (3)
Debt Investments								
U.S. Govt. Treasuries, Notes, Bonds	\$4,299,553	\$4,299,553						
U.S. Govt. TIPS	1,539,429	1,539,429						
U.S. Govt. Agencies	1,712,743		\$1,712,743					
Mortgage-Backed Govt. Pass-throughs	3,589,366	409,117						\$3,180,249
Corporate Bonds	1,933,308		80,495	\$267,782	\$1,066,627	\$518,404		
Corporate Asset-Backed	16,685					16,685		
Corporate Private Placements	150,081		9,996	69,988	27,705	42,392		
Yankee Bonds	39,780				9,641	30,139		
Supranationals	107,804		95,713	12,091				
Non-U.S. Govt./Sovereign	533,423		354,114	74,956	104,353			
Non-U.S. Corporate	285,405		172,592	9,941	51,310	51,562		
Short-Term Commercial Paper	493,731						\$493,731	
Short-Term Agencies	543,891							543,891
Total Debt Investments	\$15,245,199	\$6,248,099	\$2,425,653	\$434,758	\$1,259,636	\$659,182	\$493,731	\$3,724,140
Other Investments								
U.S. Equity	\$7,588,283		(1) Includes obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government and are not considered to have credit risk. (2) A1 is the highest rating category for commercial paper. (3) Includes securities that are implicitly guaranteed by the U.S. government, but are not rated by Standard & Poor's or Moody's.					
Non-U.S. Equity	3,688,347							
Real Estate	484,144							
Money Market Funds	27							
Total Other Investments	\$11,760,801							
Total Investments	\$27,006,000							
Less: Short-term Investments Classified as Cash Equivalents on the Statements of Plan Net Assets	(805,661)							
Total Investments as Shown on Statements of Plan Net Assets	\$26,200,339							

Investment Type	Fair Value as of 6/30/04	U.S. Treasury/ Agency (1)	Credit Quality Ratings					
			AAA	AA	A	BBB	A1 (2)	Not Rated (3)
Debt Investments								
U.S. Govt. Treasuries, Notes, Bonds	\$6,086,447	\$6,086,447						
U.S. Govt. TIPS	58,640	58,640						
U.S. Govt. Agencies	636,627		\$636,627					
Mortgage-Backed Govt. Pass-throughs	3,735,523	645,225						\$3,090,298
Corporate Bonds	1,440,631		101,313	\$200,374	\$995,688	\$143,256		
Corporate Private Placements	162,213		34,491	55,977	64,681	7,064		
Yankee Bonds	33,981				9,139	24,842		
Supranationals	96,502		96,502					
Non-U.S. Govt./Sovereign	661,789		604,334	31,271	26,184			
Non-U.S. Corporate	132,897		123,093	9,804				
Short-Term Commercial Paper	550,108						\$550,108	
Short-Term Agencies	998,565							998,565
Total Debt Investments	\$14,593,923	\$6,790,312	\$1,596,360	\$297,426	\$1,095,692	\$175,162	\$550,108	\$4,088,863
Other Investments								
U.S. Equity	\$7,567,710		(1) Includes obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government and are not considered to have credit risk. (2) A1 is the highest rating category for commercial paper. (3) Includes securities that are implicitly guaranteed by the U.S. government, but are not rated by Standard & Poor's or Moody's.					
Non-U.S. Equity	2,710,780							
Real Estate	463,383							
Money Market Funds	106							
Total Other Investments	\$10,741,979							
Total Investments	\$25,335,902							
Less: Short-term Investments Classified as Cash Equivalents on the Statements of Plan Net Assets	(1,284,977)							
Total Investments as Shown on Statements of Plan Net Assets	\$24,050,925							

(continued)

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2005 AND JUNE 30, 2004 (CONTINUED)

Credit Risk - Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Credit quality ratings for the TCRS' investments in fixed income securities as of June 30, 2005 and June 30, 2004 are included in the above schedule. Securities are rated using Standard and Poor's and/or Moody's and are presented above using the Standard and Poor's rating scale. The State Pooled Investment Fund has not obtained a credit quality rating from a nationally recognized credit ratings agency.

The TCRS' investment policy specifies that bond issues subject for purchase are investment grade bonds rated in the four highest ratings by one of the recognized rating agencies. In addition, the policy states that private placements that do not have an active secondary market shall be thoroughly researched from a credit standpoint and shall be viewed by TCRS' investment staff as having the credit quality rating equivalent of an AA rating on a publicly traded issue. For short-term investments, the TCRS' investment policy provides for the purchase of only the highest quality debt issues. Commercial paper should be rated in the highest tier by all rating agencies which rate the paper, with a minimum of two ratings required. Commercial paper cannot be purchased if a rating agency has the commercial paper on a negative credit watch. The investment policy also requires preparation of a credit analysis report on the corporation prior to purchasing commercial paper.

As noted above, the TCRS does not utilize its own bank accounts but invests in the State Pooled Investment Fund for its operating cash purposes. Required risk disclosures relative to the State Pooled Investment Fund are presented in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee Tower, 312 Eighth Avenue North, Nashville, Tennessee 37243-0298.

Concentration of Credit Risk - A concentration of investments in any one single issuer of debt securities presents a greater risk for loss in the event that the issuer fails on its obligations. The TCRS had the following investment amounts and percentages of plan net assets, in organizations representing five percent or more of plan net assets, excluding those organizations whose issues are explicitly guaranteed by the United States government, and investments in mutual funds, external investment pools, and other pooled investments:

Issuer Organization	June 30, 2005		June 30, 2004	
	Fair Value	Percentage	Fair Value	Percentage
Federal Home Loan Mortgage Corp.	\$1,988,470,907	7.31%	\$2,128,995,481	8.32%
Federal National Mortgage Assoc.	2,629,912,338	9.66%	2,242,683,999	8.77%

The TCRS' investment policy limits the maximum amount of a specific corporation's commercial paper that can be purchased to \$100 million. There are no specific investment policies that limit investment in any one issuer.

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TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2005 AND JUNE 30, 2004 (CONTINUED)

Interest Rate Risk - Interest rate risk is the risk that future changes in prevailing market rates of interest will have an adverse effect on the fair value of debt investments. The fair values of securities with long terms to maturity may be highly sensitive to interest rate changes. The TCRS' investment policy does not specifically address limits on investment maturities. The fixed income portfolio, however, is benchmarked against the Citigroup Broad Investment Grade Index and tends to have a duration within a tight range around that index. The TCRS had the following investments and effective duration at June 30, 2005 and June 30, 2004.

Debt Investments

(Expressed in Thousands)

Investment Type	Fair Value as of June 30, 2005	Effective Duration (years)
<u>Debt Investments</u>		
U.S. Govt. Treasuries, Notes, Bonds	\$4,299,553	3.87
U.S. Govt. TIPS	1,539,429	4.00
U.S. Govt. Agencies	1,712,743	2.63
Mortgage-Backed Govt. Pass-thrus	3,589,366	2.84
Corporate Bonds	1,933,308	5.63
Corporate Asset-Backed	16,685	2.16
Corporate Private Placements	150,081	3.45
Yankee Bonds	39,780	8.03
Supranationals	107,804	3.43
Non-U.S. Govt./Sovereign	533,423	6.95
Non-U.S. Corporate	285,405	6.29
Short-Term Commercial Paper	493,731	0.03
Short-Term Agencies	543,891	0.17
Total Debt Investments	\$15,245,199	3.63

Investment Type	Fair Value as of June 30, 2004	Effective Duration (years)
<u>Debt Investments</u>		
U.S. Govt. Treasuries, Notes, Bonds	\$6,086,447	4.98
U.S. Govt. TIPS	58,640	6.59
U.S. Govt. Agencies	636,627	3.43
Mortgage-Backed Govt. Pass-thrus	3,735,523	4.03
Corporate Bonds	1,440,631	4.98
Corporate Private Placements	162,213	4.12
Yankee Bonds	33,981	8.36
Supranationals	96,502	3.40
Non-U.S. Govt./Sovereign	661,789	4.43
Non-U.S. Corporate	132,897	5.15
Short-Term Commercial Paper	550,108	0.06
Short-Term Agencies	998,565	0.09
Total Debt Investments	\$14,593,923	4.12

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TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2005 AND JUNE 30, 2004 (CONTINUED)

Foreign Currency Risk - Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or deposit. The TCRS' investment policy limits the asset allocation for international investments to twenty-five percent of total assets. The TCRS' exposure to foreign currency risk at June 30, 2005 and June 30, 2004 was as follows:

Foreign Currency-Denominated Investments

(Expressed in Thousands)

Currency	Total Fair Value June 30, 2005	Fixed Income	Equity	Cash
Australian Dollar	\$209,165	\$12,039	\$197,008	\$118
British Pound Sterling	990,301	78,452	911,846	3
Canadian Dollar	5,690		5,690	
Danish Krone	73,101		73,101	
Euro Currency	1,436,934	263,623	1,173,275	36
Hong Kong Dollar	88,767		87,638	1,129
Japanese Yen	1,240,158	447,300	792,359	499
New Zealand Dollar	5,552		5,552	
Norwegian Krone	29,000		29,000	
Singapore Dollar	34,482		34,378	104
Swedish Krona	121,748		121,748	
Swiss Franc	209,949		209,949	
Total	\$4,444,847	\$801,414	\$3,641,544	\$1,889

Currency	Total Fair Value June 30, 2004	Fixed Income	Equity	Cash
Australian Dollar	\$115,554	\$10,885	\$104,670	(\$1)
Brazilian Real	5,811		5,411	400
British Pound Sterling	710,090	71,975	638,113	2
Canadian Dollar	2,791		2,791	
Chilean Peso	147		147	
Danish Krone	33,590		33,590	
Euro Currency	993,858	223,990	769,768	100
Hong Kong Dollar	69,726		69,706	20
Indian Rupee	19,314		12,939	6,375
Indonesian Rupiah	3,990		3,305	685
Japanese Yen	912,655	309,904	602,405	346
Malaysian Ringgit	14,461		12,786	1,675
Mexican Nuevo Peso	5,145		5,145	
New Taiwan Dollar	19,745		13,611	6,134
New Zealand Dollar	0			
Norwegian Krone	17,584		17,587	(3)
Philippine Peso	402		402	
Renminbi Yuan	1,045		1,045	
Singapore Dollar	18,998		18,971	27
South African Rand	9,662		9,662	
South Korean Won	45,701		33,739	11,962
Swedish Krona	72,878		72,880	(2)
Swiss Franc	145,800		147,231	(1,431)
Thai Baht	7,327		7,327	
Turkish Lira	2,216		2,216	
Total	\$3,228,490	\$616,754	\$2,585,447	\$26,289

(continued)

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2005 AND JUNE 30, 2004 (CONTINUED)

Derivatives - The international securities expose the TCRS to potential losses due to a possible rise in the value of the US dollar. The TCRS investment managers can reduce foreign currency exposure by selling foreign currency forward contracts, at agreed terms and for future settlement, usually within a year. The manager will reverse the contract by buying the foreign currency before the settlement date. A gain (loss) on this transaction pair will hedge a loss (gain) on the currency movement of the international security. The TCRS can sell up to 80% of its foreign currency exposure into US dollars. The fair value of foreign currency forward contracts outstanding as of June 30, 2005 and June 30, 2004 has been reflected in the financial statements.

Asset-Backed Securities - Mortgage-backed securities are based on cash flows from interest and principal payments on underlying mortgages. Therefore, they are sensitive to prepayments by mortgagees, which may result from a decline in interest rates. The TCRS invests in these securities primarily to enhance returns by taking advantage of opportunities available in this sector of the securities markets.

D. COMMITMENTS

Standby Commercial Paper Purchase Agreement - The TCRS has agreed to serve as standby commercial paper purchaser for commercial paper issued by the Funding Board of the State of Tennessee. By serving as a standby commercial paper purchaser, the TCRS receives an annual fee of 7.5 basis points on the \$250 million maximum issuance under this agreement during times when both Moody's and Standard and Poor's investment ratings assigned to the State of Tennessee's general obligation bonds are Aaa and AAA respectively, and 12 basis points during times when either Moody's or Standard and Poor's has assigned ratings other than Aaa and AAA respectively. In the unlikely event that the TCRS would be called upon to purchase the commercial paper, the TCRS would receive interest at a rate equal to prime plus 75 basis points during the first 30 consecutive days, plus an additional 50 basis points for each consecutive 30 days thereafter, up to a maximum rate allowed by state law.

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULES OF FUNDING PROGRESS**

SCHEDULES OF FUNDING PROGRESS*Expressed in Thousands*

	Actuarial Valuation Date	Actuarial Value of Plan Assets (a)	Actuarial Liability (AAL) Frozen Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
SETHEEPP	7/1/2003	\$ 22,099,252	\$ 22,151,745	\$ 52,493	99.76%	\$ 4,773,297	1.10%
	7/1/2001	20,760,989	20,842,216	81,227	99.61%	4,451,452	1.82%
	7/1/1999	18,327,133	18,420,156	93,023	99.49%	4,132,409	2.25%
PSPP	7/1/2003	3,605,529	3,923,475	317,946	91.90%	1,731,135	18.37%
	7/1/2001	3,187,990	3,528,137	340,147	90.36%	1,545,593	22.01%
	7/1/1999	2,690,781	2,890,942	200,161	93.08%	1,341,363	14.92%

The SETHEEPP is comprised of a number of employee groups. However, the unfunded liability of \$52.5 million at July 1, 2003 is attributable to two employee groups: 1) County Officials employed prior to July 1, 1972 and 2) State Judges and Attorneys General employed prior to July 1, 1972. The PSPP represents 418 participating entities at July 1, 2003. The unfunded liability of \$317.9 million is attributable to 353 of the 418 entities.

See accompanying Notes to Required Supplementary Information

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULES OF EMPLOYER CONTRIBUTIONS

SCHEDULES OF EMPLOYER CONTRIBUTIONS*Expressed in Thousands*

Year Ended June 30	SETHEEPP		PSP	
	Annual Required Contribution	Percentage Contributed	Annual Required Contribution	Percentage Contributed
2005	\$ 448,154	100%	\$ 181,096	100%
2004	271,298	100%	139,808	100%
2003	264,320	100%	134,014	100%
2002	243,498	100%	103,374	100%
2001	232,149	100%	103,681	100%
2000	252,162	100%	82,749	100%

An actuarial valuation of the TCRS is performed every two years with the next valuation scheduled to be effective July 1, 2005.

See accompanying Notes to Required Supplementary Information

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
AS OF JUNE 30, 2005 AND JUNE 30, 2004

The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the July 1, 2003 actuarial valuation follows.

	<u>SETHEEPP</u>	<u>PSPP</u>
Valuation Date	July 1, 2003	July 1, 2003
Actuarial cost method	Frozen Entry Age	Frozen Entry Age
Amortization method	Level Dollar	Level Dollar
Remaining amortization period	12 years closed period	(1) closed period
Asset valuation method	5-year Moving Market Average	5-year Moving Market Average
Actuarial assumptions:		
Investment rate of return	7.50%	7.50%
Projected salary increases	4.75% (3)	4.75% (3)
Includes inflation at	(2)	(2)
Cost-of-living adjustments	3.00%	3.00%
Increase in Social Security wage base	3.50%	3.50%

- (1) The length of the amortization period varies by political subdivision, not to exceed 30 years.
- (2) No explicit assumption is made regarding the portion attributable to the effect of inflation on salaries.
- (3) Uniform rate that approximates the effect of a graded salary scale.

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
SCHEDULES OF ADMINISTRATIVE EXPENSES
FOR THE YEAR ENDED JUNE 30, 2005

	SETHEEPP	PSPP	TOTAL
PERSONNEL SERVICES			
Salaries and wages	\$1,082,291	\$ 984,811	\$2,067,102
Employee benefits	343,528	312,588	656,116
TOTAL PERSONNEL SERVICES	<u>1,425,819</u>	<u>1,297,399</u>	<u>2,723,218</u>
PROFESSIONAL SERVICES			
Accounting	95,259	86,679	181,938
Actuarial services	150,112	136,592	286,704
Data processing	222,663	202,609	425,272
Disability review	0	0	0
Information systems	344,599	313,562	658,161
Management services	151,847	138,170	290,017
Medical review	21,919	19,945	41,864
Administrative, Internal Audit, Legal, Personnel	306,900	279,258	586,158
TOTAL PROFESSIONAL SERVICES	<u>1,293,299</u>	<u>1,176,815</u>	<u>2,470,114</u>
COMMUNICATION			
Travel	15,564	14,163	29,727
Telephone	26,313	23,944	50,257
Printing	25,719	23,403	49,122
Postage	100,885	91,799	192,684
TOTAL COMMUNICATION	<u>168,481</u>	<u>153,309</u>	<u>321,790</u>
MISCELLANEOUS			
Office space	79,318	72,175	151,493
Supplies and maintenance	31,661	28,810	60,471
Other services and charges	9,919	9,025	18,944
TOTAL MISCELLANEOUS	<u>120,898</u>	<u>110,010</u>	<u>230,908</u>
TOTAL ADMINISTRATIVE EXPENSES	<u>\$3,008,497</u>	<u>\$2,737,533</u>	<u>\$5,746,030</u>

With 204,735 active members and 89,772 retired members, the operating cost per member was \$19.51 for the year ended June 30, 2005.

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
SCHEDULES OF ADMINISTRATIVE EXPENSES
FOR THE YEAR ENDED JUNE 30, 2004**

	SETHEPP	PSPP	TOTAL
PERSONNEL SERVICES			
Salaries and wages	\$1,004,164	\$ 889,379	\$1,893,543
Employee benefits	273,641	242,362	516,003
TOTAL PERSONNEL SERVICES	<u>1,277,805</u>	<u>1,131,741</u>	<u>2,409,546</u>
PROFESSIONAL SERVICES			
Accounting	89,405	79,186	168,591
Actuarial services	208,815	184,946	393,761
Data processing	223,427	197,888	421,315
Disability review	55,682	49,318	105,000
Information systems	295,163	261,424	556,587
Management services	157,067	139,114	296,181
Medical review	17,871	15,829	33,700
Administrative, Internal Audit, Legal, Personnel	294,668	260,985	555,653
TOTAL PROFESSIONAL SERVICES	<u>1,342,098</u>	<u>1,188,690</u>	<u>2,530,788</u>
COMMUNICATION			
Travel	13,628	12,070	25,698
Telephone	25,524	22,606	48,130
Printing	32,295	28,604	60,899
Postage	106,224	94,081	200,305
TOTAL COMMUNICATION	<u>177,671</u>	<u>157,361</u>	<u>335,032</u>
MISCELLANEOUS			
Office space	96,981	85,896	182,877
Supplies and maintenance	31,470	27,872	59,342
Other services and charges	8,939	7,917	16,856
TOTAL MISCELLANEOUS	<u>137,390</u>	<u>121,685</u>	<u>259,075</u>
TOTAL ADMINISTRATIVE EXPENSES	<u>\$2,934,964</u>	<u>\$2,599,477</u>	<u>\$5,534,441</u>

With 200,686 active members and 86,205 retired members, the operating cost per member was \$19.29 for the year ended June 30, 2004.

TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
SCHEDULES OF INVESTMENT EXPENSES
FOR THE YEAR ENDED JUNE 30, 2005

	SETHEPP	PSPP	TOTAL
PERSONNEL SERVICES			
Salaries and wages	\$ 1,311,497	\$ 225,168	\$ 1,536,665
Employee benefits	346,203	59,439	405,642
TOTAL PERSONNEL SERVICES	<u>1,657,700</u>	<u>284,607</u>	<u>1,942,307</u>
PROFESSIONAL SERVICES			
Accounting	138,845	23,838	162,683
Legal services	87,435	15,011	102,446
Data processing	68,305	11,727	80,032
Information systems	130,639	22,429	153,068
Management services	18,943	3,252	22,195
External investment manager fees	7,101,568	1,219,256	8,320,824
Investment consulting fees	218,782	37,562	256,344
Investment custodian fees	724,972	124,469	849,441
Real estate manager fees	2,827,290	485,412	3,312,702
Administrative, Internal Audit, Personnel	274,292	47,093	321,385
TOTAL PROFESSIONAL SERVICES	<u>11,591,071</u>	<u>1,990,049</u>	<u>13,581,120</u>
COMMUNICATION			
Travel	9,007	1,546	10,553
Telephone	15,463	2,655	18,118
Printing	2,104	361	2,465
Postage	3,296	566	3,862
TOTAL COMMUNICATION	<u>29,870</u>	<u>5,128</u>	<u>34,998</u>
MISCELLANEOUS			
Office space	58,171	9,987	68,158
Supplies and maintenance	27,021	4,639	31,660
Other services and charges	30,420	5,223	35,643
TOTAL MISCELLANEOUS	<u>115,612</u>	<u>19,849</u>	<u>135,461</u>
TOTAL INVESTMENT EXPENSES	<u>\$13,394,253</u>	<u>\$ 2,299,633</u>	<u>\$15,693,886</u>

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
SCHEDULES OF INVESTMENT EXPENSES
FOR THE YEAR ENDED JUNE 30, 2004**

	SETHEEPP	PSPP	TOTAL
PERSONNEL SERVICES			
Salaries and wages	\$ 1,177,425	\$ 195,709	\$ 1,373,134
Employee benefits	274,961	45,703	320,664
TOTAL PERSONNEL SERVICES	<u>1,452,386</u>	<u>241,412</u>	<u>1,693,798</u>
PROFESSIONAL SERVICES			
Accounting	126,320	20,997	147,317
Legal services	83,233	13,835	97,068
Data processing	80,826	13,435	94,261
Information systems	111,078	18,463	129,541
Management services	8,743	1,453	10,196
External investment manager fees	6,902,631	1,147,344	8,049,975
Investment consulting fees	242,585	40,322	282,907
Investment custodian fees	713,210	118,548	831,758
Real estate manager fees	2,038,144	338,777	2,376,921
Administrative, Internal Audit, Personnel	238,491	39,641	278,132
TOTAL PROFESSIONAL SERVICES	<u>10,545,261</u>	<u>1,752,815</u>	<u>12,298,076</u>
COMMUNICATION			
Travel	11,319	1,881	13,200
Telephone	15,731	2,615	18,346
Printing	3,081	512	3,593
Postage	3,309	550	3,859
TOTAL COMMUNICATION	<u>33,440</u>	<u>5,558</u>	<u>38,998</u>
MISCELLANEOUS			
Office space	72,322	12,021	84,343
Supplies and maintenance	8,884	1,477	10,361
Other services and charges	293,406	48,769	342,175
TOTAL MISCELLANEOUS	<u>374,612</u>	<u>62,267</u>	<u>436,879</u>
TOTAL INVESTMENT EXPENSES	<u><u>\$12,405,699</u></u>	<u><u>\$ 2,062,052</u></u>	<u><u>\$14,467,751</u></u>

**TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
SCHEDULES OF EXPENSES FOR CONSULTANTS
FOR THE YEARS ENDED JUNE 30, 2004 AND JUNE 30, 2005**

FOR THE YEAR ENDED JUNE 30, 2005

	SETHEEPP	PSPP	TOTAL
ACTUARIAL SERVICES			
Bryan, Pendleton, Swats and McAllister	<u>\$150,112</u>	<u>\$136,592</u>	<u>\$286,704</u>
MEDICAL REVIEW SERVICES			
Bramlett and Associates	183	167	350
Suzanne Fletcher, M.D.	6,402	5,826	12,228
Barry Siegel, M.D.	8,931	8,127	17,058
Medical Specialists of Knoxville	<u>6,403</u>	<u>5,825</u>	<u>12,228</u>
TOTAL MEDICAL REVIEW SERVICES	<u>21,919</u>	<u>19,945</u>	<u>41,864</u>
TOTAL EXPENSES FOR CONSULTANTS	<u><u>\$172,031</u></u>	<u><u>\$156,537</u></u>	<u><u>\$328,568</u></u>

Note: For information regarding fees paid to investment professionals, refer to the Investment Section of this report.

FOR THE YEAR ENDED JUNE 30, 2004

	SETHEEPP	PSPP	Total
ACTUARIAL SERVICES			
Bryan, Pendleton, Swats and McAllister	<u>\$208,815</u>	<u>\$184,946</u>	<u>\$393,761</u>
MEDICAL REVIEW SERVICES			
William Bailey, M.D.	370	330	700
Suzanne Fletcher, M.D.	6,364	5,636	12,000
Barry Siegel, M.D.	6,364	5,636	12,000
Jeffrey Summers, M.D.	<u>4,773</u>	<u>4,227</u>	<u>9,000</u>
TOTAL MEDICAL REVIEW SERVICES	<u>17,871</u>	<u>15,829</u>	<u>33,700</u>
DISABILITY REVIEW SERVICES			
Kroll Background America	<u>55,682</u>	<u>49,318</u>	<u>105,000</u>
TOTAL EXPENSES FOR CONSULTANTS	<u><u>\$282,368</u></u>	<u><u>\$250,093</u></u>	<u><u>\$532,461</u></u>

Note: For information regarding fees paid to investment professionals, refer to the Investment Section of this report.

INVESTMENT SECTION

“...an equal participation in the free navigation of the Mississippi is one of the inherent rights of the citizens of this state; it cannot, therefore, be conceded to any prince, potentate, power, person or persons whatever.”
Tennessee Constitution, 1796

The Tennessee River system is the

The first steamboat on the Cumberland was

An estimated 100,000 board-feet of hardwood logs floated in the early 19th century on the Cumberland system. The South Fork, Wolf, Obey, and the Tennessee Fork River

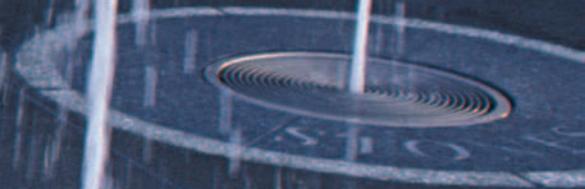
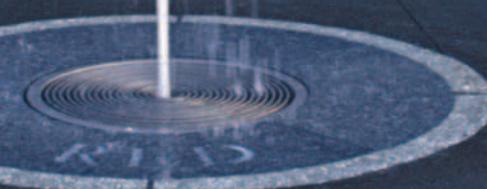
Beautiful cypress and tupelo haunt the hardwood bottomlands of the Hatchie and the Wolf.

Tennessee is the only state for navigable water in the state and it drains 400,000 square miles over a 7 state area.

Over 10% of Tennessee's 313 species of fish show trends toward extinction.

Pre-Columbian era (9000-1600A.D.) mounds at the confluence of the Cumberland, French, and Tennessee, Little Tennessee, Obion, and

“...the basin of the Mississippi



REPORT BY INVESTMENT CONSULTANT

STRATEGIC INVESTMENT SOLUTIONS, INC.

333 BUSH STREET, STE. 2000
SAN FRANCISCO, CALIFORNIA 94104

TEL 415/362-3484 ■ FAX 415/362-2752

November 11, 2005

Mr. Eddie W. Hennessee
Executive Director
Tennessee Consolidated Retirement System
Fifth and Deadrick, 10th Floor
Andrew Jackson Building
Nashville, TN 37243 0230

Dear Ed:

Strategic Investment Solutions prepares the quarterly performance reports in full compliance with AIMR standards. For the year ended June 30, 2005, global equity and fixed income markets continued to post positive results with the TCRS composite up 7.26%. Domestic equities were led by smaller capitalization and value oriented stocks while international equities were boosted by strong global economic growth and a declining dollar. Corporate and mortgage bonds performed well.

As of June 30, 2005, the System's asset allocation and one year respective returns were:

Asset Class	% of Assets	One Year Return
Domestic Equities	28.0%	7.25%
Traditional Fixed Income	42.0%	6.18%
International Equities	14.0%	12.58%
International Fixed Income	3.0%	6.07%
Cash and Equivalents	3.7%	2.04%
Real Estate	1.6%	14.80%
Inflation Indexed Fixed Income	7.8%	6.64%
Total	100.0%	7.26%

TCRS underperformed the median fund in the ICC Universe of Public Plan Sponsors (> \$100 million) over the past one and three years. This was the result of the System's high fixed income allocation relative to other large public funds in an environment of strong domestic and international equity market returns. Real estate holdings aided returns. The overall asset allocation is geared not to maximize absolute returns but to meet the System's liabilities while minimizing the risk of loss.

Over the next five years SIS expects most asset class returns to fall within the mid-to-high single digits, accompanied by moderate economic growth and inflation. This will continue to make it difficult to achieve high absolute returns though the overall volatility in most capital markets remains low by historical standards.

SIS was recently hired as the System's investment consultant in early 2005. We are an independent, employee-owned firm and provide strategic consulting services to large institutional investors, including nine state-sponsored systems.

Please feel free to call me should you have any questions.

Best regards,



Peter A. Keliuotis, CFA

LETTER FROM TCRS CHIEF INVESTMENT OFFICER

STATE OF TENNESSEE

DALE SIMS
STATE TREASURER



THOMAS G. MILNE
CHIEF INVESTMENT
OFFICER

TREASURY DEPARTMENT
TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
11TH FLOOR ANDREW JACKSON STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243

November 7, 2005

Dear Members:

I am pleased to present the Investment Section of the TCRS Comprehensive Annual Financial Report for the fiscal year ended June 30, 2005.

With over \$27 billion in assets, TCRS is one of the largest public pension plans in the United States. TCRS assets are invested to preserve principal value, to achieve a superior rate of return within acceptable risk levels, and to provide the liquidity necessary to pay beneficiaries in a timely manner.

The TCRS portfolio is diversified among domestic and international stocks and bonds, real estate, and short-term securities. A diversified portfolio is used to manage risk and minimize significant exposure to unpredictable events. The TCRS consultant periodically prepares an asset allocation study to determine the optimal long-term mix of assets to best meet the plans investment objectives. TCRS has adopted a conservative investment strategy that has yielded excellent returns with a low level of risk.

I am proud to report that the TCRS earned 7.26% for the year ended June 30, and earned 7.76% annually for the ten year period ended June 30, 2005.

The experienced TCRS investment staff is committed to providing superior investment returns in a financially sound manner with the highest ethical and professional standards. With the leadership of our Board and the work of our dedicated staff, this goal will be met.

Sincerely,

A handwritten signature in cursive script that reads "Thomas G. Milne".

Thomas G. Milne

STATUTORY INVESTMENT AUTHORITY

STATUTORY INVESTMENT AUTHORITY

The investment authority of TCRS is prescribed in the *Tennessee Code Annotated*, Title 8, Chapter 37. This chapter provides that, with certain enumerated exceptions, investments of TCRS assets are subject to the same terms, conditions and limitations imposed on domestic life insurance companies as set forth in *T.C.A.*, Section 56, Chapter 3. The Board of Trustees of TCRS adopts investment policy relative to the investment of TCRS assets. The investment objective is to obtain the highest available return on investments consistent with the preservation of principal while maintaining sufficient liquidity to react to the changing environment and to pay beneficiaries in a timely manner. A summary of statutory and policy provisions follow.

DOMESTIC STOCKS

- ❖ No more than 50% of the TCRS portfolio may be invested in common stock, preferred stock and convertible bonds.
- ❖ No more than 4.99% of the outstanding shares of any one company may be purchased.

DOMESTIC FIXED INCOME

- ❖ No more than 75% of the TCRS portfolio may be invested in fixed income securities exceeding one year.
- ❖ Only issues that are investment grade securities (four highest ratings) may be purchased.
- ❖ Private placements are limited to 15% of the domestic fixed income portfolio. Private placements may be purchased if staff evaluation determines that the credit quality is equivalent to double A.

INTERNATIONAL

- ❖ Combined International equity and fixed income investments are limited to 25% of the TCRS portfolio.

INTERNATIONAL EQUITY

- ❖ No more than 25% of the TCRS portfolio may be invested in international equity securities.
- ❖ Canadian securities shall be treated as domestic securities for policy purposes.
- ❖ The countries in the Morgan Stanley Capital International EAFE index have been approved by the Board for international investing.

INTERNATIONAL FIXED INCOME

- ❖ No more than 10% of TCRS portfolio may be invested in international fixed income securities.
- ❖ Investments are limited to seven major developed countries.

SHORT-TERM SECURITIES

- ❖ Commercial paper should be rated A1 or P1.

STOCK OPTIONS AND BOND FUTURES

- ❖ Limited to 10% of the portfolio.
- ❖ Only covered call options may be written.

DOMESTIC STOCK INDEX FUTURES

- ❖ Contracts shall not exceed 5% of the TCRS portfolio.
- ❖ Shall only be used for asset allocation purposes and not for speculative leveraging. The system's cash and short-term securities must exceed the amount of the contract obligation.

SECURITIES LENDING

- ❖ May not lend more than 30% of the portfolio.
- ❖ Collateral, other than cash, must have a market value of 102% of the security loaned.

STANDBY NOTE PURCHASE AGREEMENT

- ❖ TCRS may enter into contracts to serve as a standby note purchaser for the Tennessee State School Bond Authority, the Tennessee State Funding Board and the Tennessee Local Development Authority.

FOREIGN CURRENCY HEDGING

- ❖ May not exceed 80% of the international securities.

REAL ESTATE

- ❖ No more than 5% of the TCRS portfolio may be invested in real estate.

PROXY VOTING

- ❖ Shall vote proxies in a manner which will provide the best ultimate value to shareholders.

INVESTMENT PERFORMANCE REVIEW

INVESTMENT PERFORMANCE REVIEW

Periods Ending June 30, 2005

	Annualized Returns		
	Current Year	3-Year	5-Year
Pension Plan Portfolio			
TCRS Performance	7.26 %	7.15 %	3.49 %
Benchmark - Public Fund Index Median	9.38 %	9.50 %	3.73 %
Domestic Equity			
TCRS Performance	7.25 %	8.63 %	(2.04)%
Benchmark - S & P 1500	7.24 %	8.60 %	(1.21)%
- Dow Jones Industrial Average	0.65 %	5.90 %	1.71 %
- S & P 500	6.33 %	8.29 %	(2.37)%
Domestic Fixed Income			
TCRS Performance	6.18 %	5.57 %	7.28 %
Benchmark - Lehman Aggregate (excluding BBB)	6.60 %	5.41 %	7.26 %
Inflation Hedged Bonds	6.64 %	-	-
International Equity			
TCRS Performance	12.58 %	12.78 %	1.24 %
Benchmark - MSCI EAFE Index	14.13 %	12.96 %	0.17 %
International Fixed Income			
TCRS Performance	6.07 %	10.32 %	6.54 %
Citigroup G5 - ex US Index	5.78 %	8.83 %	5.85 %
Real Estate			
TCRS Performance	14.80 %	10.03 %	9.19 %
Benchmark - NCREIF Index	15.55 %	10.75 %	10.15 %
Short-Term Securities			
TCRS Performance	2.04 %	1.53 %	2.62 %
Benchmark - Three month Treasury Bill	2.16 %	1.56 %	2.62 %

	Strategic Investment Solutions
	Percentile Rankings Risk Adjusted Basis
Ranking of TCRS Portfolio	
Last five years	44
Last ten years	18

The percentile ranking is the position of the TCRS portfolio as compared with other public funds with 1 being the best and 100 being the worst. The investment performance for TCRS was computed using a market, time weighted rate of return by an independent investment consultant for TCRS in accordance with the AIMR

ASSET ALLOCATION**ASSET ALLOCATION***as of June 30, 2005**Expressed in Thousands*

Asset Class	Fair Value	Percentage
Domestic Equity	\$ 7,588,283	28%
Domestic Fixed	13,406,163	50%
International Equity	3,688,347	13%
International Fixed Income	801,414	3%
Short-term Securities	1,037,649	4%
Real Estate	<u>484,144</u>	<u>2%</u>
Total	<u>\$ 27,006,000</u>	<u>100%</u>

This schedule classifies convertible bonds as fixed income securities and preferred stock as fixed income securities. For investment purposes, convertible bonds and preferred stock are considered equity securities. In addition, inflation hedged bonds are not presented as a separate asset class on the above schedule. Accordingly, the asset allocation percentages in this schedule will vary from the investment consultant's asset allocation percentages.

LARGEST HOLDINGS

JUNE 30, 2005

Largest Stock Holdings
By Fair Value
as of June 30, 2005

Shares	Security Name	Fair Value
4,681,594	EXXON MOBIL CORPORATION	\$ 269,051,207
7,380,300	GENERAL ELECTRIC COMPANY	255,727,395
7,369,000	MICROSOFT CORPORATION	183,045,960
3,460,006	CITIGROUP INCORPORATED	159,956,077
2,235,000	JOHNSON & JOHNSON	145,275,000
5,156,620	PFIZER INCORPORATED	142,219,580
3,097,148	BANK OF AMERICA CORPORATION	141,260,920
4,778,000	INTEL CORPORATION	124,514,680
2,550,000	WAL-MART STORES INCORPORATED	122,910,000
1,738,000	CHEVRON CORPORATION	97,188,960

Largest Bond Holdings
By Fair Value
as of June 30, 2005

Par Value	Security Name	Yield	Maturity	Moody's Quality Rating	Fair Value
1,170,000,000	UNITED STATES TREASURY NOTES	3.64%	01/31/2007	Aaa	\$ 1,160,768,700
500,000,000	UNITED STATES TREASURY INFL IDX NOTE	1.25%	01/15/2007	Aaa	633,494,253
600,000,000	UNITED STATES TREASURY NOTES	3.51%	05/15/2006	Aaa	617,202,000
500,000,000	UNITED STATES TREASURY NOTES	3.65%	02/15/2008	Aaa	491,895,000
500,000,000	UNITED STATES TREASURY NOTES	3.70%	04/15/2009	Aaa	489,980,000
400,000,000	UNITED STATES TREASURY INFL IDX N/B	1.38%	04/15/2010	Aaa	400,650,367
300,000,000	UNITED STATES TREASURY NOTES	3.81%	05/15/2013	Aaa	296,181,000
200,000,000	UNITED STATES TREASURY NOTES INDEX	1.47%	01/15/2012	Aaa	244,709,255
150,000,000	UNITED STATES TREASURY BONDS	4.22%	02/15/2021	Aaa	212,326,500
160,000,000	UNITED STATES TREASURY BONDS	4.04%	05/15/2016	Aaa	204,881,600

A complete portfolio listing is available upon request.

Key to Ratings: All ratings presented are from Moody's Investors Service with the exception of some of the government agency securities. Moody's does not rate these securities. Standard & Poor's does provide ratings for the securities (AAA is Standard & Poor's highest rating.) Government Securities are not rated per se' but are considered the best quality securities.

Moody's rates securities as follows:

- Aaa: Best Quality
- Aa: High Quality
- A: Upper Medium Quality
- Baa: Medium Quality

I N V E S T M E N T S U M M A R Y

I N V E S T M E N T S U M M A R Y

as of June 30, 2005

	Domestic		International		Total	
	Fair Value	%	Fair Value	%	Fair Value	%
Fixed Income						
Government Bonds	\$11,153,495,797	41.30%	\$ 533,108,524	1.97%	\$11,686,604,321	43.27%
Corporate Bonds	2,252,668,331	8.34%	268,304,976	1.00%	2,520,973,307	9.34%
Total Fixed Income	<u>13,406,164,128</u>	<u>49.64%</u>	<u>801,413,500</u>	<u>2.97%</u>	<u>14,207,577,628</u>	<u>52.61%</u>
Common Stock						
Capital Goods & Services	124,884,698	0.46%	48,271,921	0.18%	173,156,619	0.64%
Consumer Durables	100,034,741	0.37%	14,174,513	0.05%	114,209,254	0.42%
Consumer Non-Durables	1,765,219,525	6.54%	259,939,644	0.96%	2,025,159,169	7.50%
Energy	671,088,091	2.48%	200,208,649	0.74%	871,296,740	3.22%
Financial	1,475,729,806	5.47%	2,366,700,998	8.77%	3,842,430,804	14.24%
Materials & Services	1,541,136,267	5.71%	274,710,524	1.02%	1,815,846,791	6.73%
Miscellaneous Common Stock	3,272,900	0.01%	0	0.00%	3,272,900	0.01%
Real Estate Investment Trust	32,745,910	0.12%	0	0.00%	32,745,910	0.12%
Rights	0	0.00%	54,244	0.00%	54,244	0.00%
Technology	1,239,502,355	4.59%	180,271,430	0.67%	1,419,773,785	5.26%
Transportation	106,288,752	0.39%	76,661,609	0.28%	182,950,361	0.67%
Utilities	528,380,017	1.96%	267,353,590	0.99%	795,733,607	2.95%
Total Common Stock	<u>7,588,283,062</u>	<u>28.10%</u>	<u>3,688,347,122</u>	<u>13.66%</u>	<u>11,276,630,184</u>	<u>41.76%</u>
Short-Term Investments						
Commercial Paper	493,730,802	1.83%	0	0.00%	493,730,802	1.83%
Pooled Funds & Mutual Funds	27,095	0.00%	0	0.00%	27,095	0.00%
U.S. Government Securities	543,890,973	2.01%	0	0.00%	543,890,973	2.01%
Total Short-Term Investments	<u>1,037,648,870</u>	<u>3.84%</u>	<u>0</u>	<u>0.00%</u>	<u>1,037,648,870</u>	<u>3.84%</u>
Real Estate	484,143,880	1.79%	0	0.00%	484,143,880	1.79%
Total Investments	<u>22,516,239,940</u>	<u>83.37%</u>	<u>4,489,760,622</u>	<u>16.63%</u>	<u>27,006,000,562</u>	<u>100.00%</u>
Short-Term Investments Classified as Cash Equivalents	<u>(805,660,518)</u>		<u>0</u>		<u>(805,660,518)</u>	
Total Investments as Shown on the Statement of Plan Net Assets	<u>\$21,710,579,422</u>		<u>\$4,489,760,622</u>		<u>\$26,200,340,044</u>	

This schedule classifies Canadian investments as domestic securities, convertible bonds as fixed income securities, and preferred stock as fixed income securities. For investment purposes convertible bonds and preferred stock are considered equity securities. Accordingly, the asset allocation percentages in this schedule will vary from the investment consultant's asset allocation percentages.

**SCHEDULES OF INVESTMENT FEES AND COMMISSIONS
FOR THE YEAR ENDED JUNE 30, 2005**

SCHEDULES OF FEES

	Average Assets Under Management	Fees
Asset Management		
INTERNATIONAL INVESTMENT MANAGER FEES	3.1 Billion	\$ 8,320,824
REAL ESTATE ASSET MANAGEMENT	445 Million	3,312,702
Total Asset Management		<u><u>\$11,633,526</u></u>
Other Investment Services Fees		
CUSTODIAN BANK	26.4 Billion	\$ 886,407
GENERAL INVESTMENT CONSULTANT	26.4 Billion	167,500
REAL ESTATE INVESTMENT CONSULTANT	445 Million	100,000
Total Investment Services Fees		<u><u>\$ 1,153,907</u></u>

SCHEDULES OF COMMISSIONS

Domestic Exchange Traded Shares

Broker Name	Domestic		
	Shares Traded	Commissions	Commission Per Share
A.G. EDWARDS & SONS, INC.	5,852,900	\$ 261,230	\$0.0446
BANC OF AMERICA SECURITIES	7,107,687	315,215	0.0443
BEAR STEARNS / FACTSET	4,748,400	200,316	0.0422
BEAR STEARNS & COMPANY	12,778,055	547,386	0.0428
BANK OF NEW YORK BROKERAGE, INC.	9,520,687	142,810	0.0150
CIBC WORLD MARKETS CORPORATION	6,019,450	270,763	0.0450
CITIGROUP, INC.	15,385,776	635,693	0.0413
CAPITAL INSTITUTIONAL SERVICES, INC.	15,615,065	780,753	0.0500
INSTINET, LLC	16,495,305	332,481	0.0202
JEFFERIES AND COMPANY, INC.	7,101,418	312,138	0.0440
LEHMAN BROTHERS, INC.	12,308,865	524,916	0.0426
MORGAN (J.P.) SECURITIES, INC.	4,460,550	202,908	0.0455
MORGAN KEEGAN & COMPANY, INC.	5,224,498	225,965	0.0433
PRUDENTIAL SECURITIES	9,091,308	388,206	0.0427
SANFORD C BERNSTEIN & COMPANY, LLC	5,585,400	252,330	0.0452
WILLIAM O'NEIL & COMPANY, INC.	2,430,400	104,650	0.0431
Other Brokers*	24,913,729	1,061,410	0.0426
Totals	<u><u>164,639,493</u></u>	<u><u>\$ 6,559,170</u></u>	

Program Trades where total commission cost includes trading commission, liquidity fees, and market impact fees.

Broker Name	Domestic		
	Shares Traded	Commissions	Commission Per Share
LEHMAN BROTHERS	35,610,000	\$ 1,493,004	\$0.0419
BANC OF AMERICA SECURITIES	17,795,100	623,610	0.0350
Totals	<u><u>53,405,100</u></u>	<u><u>\$ 2,116,614</u></u>	

International Exchange Traded Shares

Broker Name	International		
	Shares Traded	Commissions	Commission Per Share
ABN AMRO SECURITIES INC.	11,522,886	\$ 172,943	\$0.0150
CITIGROUP GLOBAL MKT SG SEC PTE LTD	124,436,683	172,339	0.0014
CREDIT SUISSE FIRST BOSTON CORPORATION	38,868,552	315,298	0.0081
DEUTSCHE BANC SECURITIES INC, NY	96,959,276	172,986	0.0018
GOLDMAN, SACHS AND COMPANY	34,572,461	139,473	0.0040
HSBC SECURITIES USA INC.	8,677,019	213,856	0.0246
JP MORGAN STANLEY SECURIT PVT LTD	10,292,671	109,432	0.0106
MERRILL LYNCH PIERCE FENNER + SMITH	429,472,033	354,585	0.0008
MORGAN STANLEY AND COMPANY	18,697,160	174,587	0.0093
UBS SECURITIES LLC	41,368,591	278,731	0.0067
Other Brokers*	526,160,418	1,409,768	0.0027
Totals	<u><u>1,341,027,750</u></u>	<u><u>\$ 3,513,998</u></u>	

Shares for international stocks are based on the actual foreign shares traded while the commission is expressed in U.S. dollars. Therefore, commissions per share between domestic and international are not comparable.

*Less than \$100,000 total commission per brokerage firm.

ACTUARIAL SECTION



photo by Jed DeKalb

ACTUARIAL INTRODUCTION**BIENNIAL ACTUARIAL VALUATIONS**

Biennial actuarial valuations of the TCRS are performed by an independent actuarial consulting firm to assess the funding status of the system and to determine employer contribution rates for its various components. The valuation performed as of July 1, 2003, set employer rates effective July 1, 2004. The Board of Trustees of the system is responsible for adopting the employer contribution rates after reviewing the actuarial results. The next valuation, performed as of July 1, 2005, will establish new employer rates effective July 1, 2006.

FUNDING OF PENSIONS

It is the policy of the state to fund pensions by actuarially determined contributions which are intended to provide funding for both the normal liability cost and the unfunded actuarial accrued liability cost. This policy seeks to ensure that sufficient assets will be available to pay benefits as they are due.

ACCRUED LIABILITY

With the 2003 actuarial valuation, the accrued liability, which was frozen in 1981 was again reestablished. This was accomplished by setting the unfunded accrued liability equal to the excess of the Entry Age Normal Past Service Liability over the valuation assets for each group. This action affected local government employers and two minor closed groups.

SPECIFICS

Valuations are based on demographic data (employee ages, salaries and service credits), economic projections (salary increases, interest rates and investment earnings), and decrement estimates (mortality and disability rates).

The economic projections and decrement estimates used for valuation purposes utilized the assumptions recommended by the actuary and adopted by the Board of Trustees based on an actuarial experience study conducted every four

years. The earnings rate assumption adopted by the Board is subject to the approval of the Council on Pensions and Insurance.

QUADRENNIAL EXPERIENCE STUDY

A quadrennial experience study was conducted as of June 30, 2000. A number of changes were made to the economic and decrement assumptions. The salary assumption was changed to a graded scale that reflects plan experience, while the increase in the Social Security wage base assumption was reduced to three and one-half percent. Preretirement and post-retirement mortality assumptions were also modified to more closely reflect past experience. Assumptions developed from the June 30, 2004 experience study will be used in the July 1, 2005 actuarial valuation.

ACTUARY'S CERTIFICATION LETTER

November 7, 2005

Mr. Dale Sims
Chairman, Board of Trustees
Tennessee Consolidated Retirement System
Tenth Floor
Andrew Jackson State Office Building
Nashville, Tennessee 37243-0230

Dear Mr. Sims:

Re: Actuary's Certification Letter

The purpose of this letter is to certify the actuarial adequacy of contributions being made by the State of Tennessee and participating Political Subdivisions to the Tennessee Consolidated Retirement System and to discuss the approach currently being taken toward meeting the financing objectives of the Plan.

The most recent biennial actuarial valuation of the Tennessee Consolidated Retirement System was performed as of July 1, 2003. That valuation was based on a set of actuarial assumptions (described in detail in the section headed "Summary of Actuarial Methods and Assumptions") which was adopted by the Board of Trustees on the recommendation of the actuary, as a result of a study of actual experience under the TCRS during the four year period ending June 30, 2000. The experience study concluded that the assumed rate of return and inflation assumption should remain unchanged. Modifications were recommended for many of the demographic assumptions including changes to more conservative mortality, termination and retirement rates. For Consolidated State and Political Subdivision groups, one third of the effect of termination/retirement rates was recognized as of both July 1, 2001 and July 1, 2003 with the remainder to be recognized in July 1, 2005 actuarial valuation. The salary increase rate was altered from a uniform 5.5% annual rate to a graded scale that reflects the plan experience pattern of declining escalation rates as participant ages increase.

There have been no significant changes in the level of benefits provided by the plan since the date of the preceding valuation.

The Board of Trustees in 1975 established as its financing objective the amortization of unfunded accrued liabilities over the ensuing 40-year period. In the years since then, the implementation of that general goal has involved a gradual strengthening of the methods utilized in computing required annual contributions. This has been accomplished by such steps as (1) taking advance funding of expected cost-of-living increases into account, (2) placing all amortization payments on a "level dollar" basis—a stronger basis than the "percentage of payroll" method previously utilized and (3) elimination of the unfunded accrued liability for the major contribution classes, primarily as a result of actuarial gains attributable to favorable investment performance.

In performing the 2003 valuation, we relied on employee data and asset information provided by the administrative staff of the Tennessee Consolidated Retirement System. In the case of employee data, each individual record was audited thoroughly for reasonableness and internal consistency, although the

5301 Virginia Way • Suite 400 • Brentwood, Tennessee 37027

(continued)

ACTUARY'S CERTIFICATION LETTER
(CONTINUED)

Mr. Dale Sims
November 7, 2005
Page Two

validity of the information was not traced to source documents. With respect to plan assets, a general review for consistency with the information furnished for prior valuations was performed.

Certain tables presented in the Comprehensive Financial Annual Report are derived from the July 1, 2003 actuarial valuation report prepared by Bryan, Pendleton, Swats and McAllister, LLC. The tables were prepared by the staff of the Tennessee Consolidated Retirement System and examined by our firm. These tables include the following –

Financial Section

- Schedules of Funding Progress

Actuarial Section

- Summary of Actuarial Assumptions and Methods
- Actuarial Data (current year data)
- Actuarial Balance Sheet
- Short-Term Solvency Test
- Summary of Unfunded Accrued Liabilities and Selected Funding Information
- Analysis of Financial Experience

The Schedule of Retired Member Activity in the Actuarial Section of the report was prepared by our firm using information gathered from the 1995, 1997, 1999, 2001 and 2003 actuarial valuations.

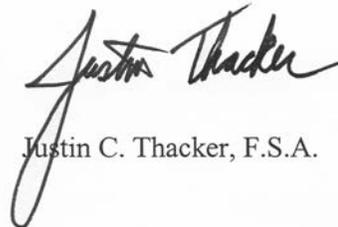
The 2003 valuation was prepared in accordance with accepted actuarial principles of practice prescribed by the Actuarial Standards Board and the principles of Governmental Accounting Standards Board Statement 25. I am a Member of the American Academy of Actuaries with experience in performing valuations for public retirement systems; all calculations were performed either by me or by other qualified actuaries under my direct supervision.

Based upon the valuation results and the contribution rates adopted by the Board of Trustees, it is our opinion that the Tennessee Consolidated Retirement System continues to fund its liabilities in accordance with standard actuarial principles of advance funding, continuing a program first adopted in 1975.

Sincerely,



Anthony S. Johnston, F.S.A.



Justin C. Thacker, F.S.A.

SUMMARY OF ACTUARIAL ASSUMPTIONS AND METHODS

The following assumptions were adopted by the Board of Trustees for use beginning with the July 1, 2001 valuation based on the consulting actuary’s recommendations resulting from the June 30, 2000 actuarial experience study.

GENERAL ACTUARIAL METHODS

- ❖ *Actuarial Cost Method* (Frozen Entry Age)—Unfunded accrued liabilities are being funded over a 40-year period commencing in 1975. The unfunded accrued liability was reestablished as part of the July 1, 2001 valuation. This was accomplished by setting the unfunded accrued liability equal to the excess (if any) of the Entry Age Normal Past Service Liability over the valuation assets for each group or zero.
- ❖ *Treatment of Actuarial Gains and Losses*—Under the Frozen Entry Age Method, any actuarial gains or losses are absorbed into the normal cost.
- ❖ *Asset Valuation Method*—Assets are valued on a basis which reflects a five-year moving average of the fair market value. Investment losses are applied to offset accumulated investment gains prior to determining the amount of earnings to be phased in.
- ❖ *Valuation Data*—The administrative staff of TCRS furnishes the actuary with demographic data relating to the active life members and the retired life members. The fair value of system assets are also provided by retirement system staff. All data is reviewed for reasonableness and consistency from year to year, but is not audited by the actuary.
- ❖ *Post-Retirement Adjustments*—Retirement benefits are assumed to increase at the maximum geometric rate of 3% annually, reflecting the 1997 adoption of compounded cost-of-living adjustments.

ECONOMIC ASSUMPTIONS

- ❖ *Investment Return Rate*—Seven and one-half percent per annum, compounded annually.
- ❖ *Employee Salary Increases*—Graded scale that reflects the plan experience pattern of declining escalation rates as participant ages increase. No explicit assumption is made regarding the portion attributable to the effects of inflation on salaries. Active membership is assumed to remain constant.
- ❖ *Increase in Social Security Wage Base*—Three and one-half percent annual increase.

DECREMENT ASSUMPTIONS

- ❖ *Post-Retirement Mortality*—Annuity mortality tables previously used are no longer compatible with TCRS results. Specifically adopted tables have been created to more accurately reflect patterns that occur among TCRS retirees. Sample rates are below.

	Male	Female
<i>Teachers</i>		
Age 50	0.3%	0.2%
Age 60	0.7%	0.5%
Age 70	2.1%	1.3%
<i>State & Political Subdivisions</i>		
Age 50	0.4%	0.2%
Age 60	1.2%	0.6%
Age 70	3.2%	1.7%

- ❖ *Preretirement Mortality*—The 1994 Group Annuity mortality table is used for state employees and political subdivision employees. For teachers, the 1983 Group Annuity Mortality Table is used with an adjustment of 60% for females and 50% for males.

- ❖ *Withdrawal Due to Disability*—Sample rates of disability based on experience:

	Male	Female
<i>Teachers</i>		
Age 30	0.03%	0.03%
Age 40	0.09%	0.09%
Age 50	0.17%	0.17%
<i>State</i>		
Age 30	0.05%	0.05%
Age 40	0.16%	0.17%
Age 50	0.35%	0.37%
<i>Political Subdivisions</i>		
Age 30	0.05%	0.04%
Age 40	0.14%	0.08%
Age 50	0.53%	0.36%

- ❖ *Turnover Assumption*—Tables for probabilities of separation due to termination of employment are developed utilizing a “two-year select and ultimate” approach.

(continued)

**SUMMARY OF ACTUARIAL ASSUMPTIONS AND METHODS
(CONTINUED)**

<i>Teachers</i>				<i>Retirement – The probabilities of retirement for members eligible to retire:</i>			
	1st Year Employment	2nd Year Employment	Ultimate	Age	Teachers	State	P.S.
<i>Male</i>				Age 60	15.0%	9.0%	10.0%
Age 30	15.0%	12.0%	5.6%	Age 61	22.0%	12.0%	17.0%
Age 40	15.0%	12.0%	1.5%	Age 62	26.0%	23.0%	26.0%
Age 50	15.0%	12.0%	2.0%	Age 63	22.0%	15.0%	17.0%
<i>Female</i>				Age 64	31.0%	18.0%	19.0%
Age 30	15.0%	12.0%	8.1%	Age 65	43.0%	34.0%	29.0%
Age 40	15.0%	12.0%	1.8%	Age 70	100.0%	21.0%	20.0%
Age 50	15.0%	12.0%	1.8%	Age 75	100.0%	100.0%	100.0%
 <i>State Employees</i>				<p>In addition, for members younger than age 60, a loading factor of 10 percent is added during the year the member is first eligible for unreduced retirement. After age 60, for those members with 15 or more years of service, a 10% load is added for teachers and 5% for state employees and political subdivision employees.</p>			
	1st Year Employment	2nd Year Employment	Ultimate				
<i>Male</i>							
Age 30	27.2%	23.1%	10.7%				
Age 40	23.1%	16.7%	4.8%				
Age 50	16.5%	14.0%	2.9%				
<i>Female</i>							
Age 30	27.2%	23.1%	10.7%				
Age 40	23.1%	16.7%	4.8%				
Age 50	16.5%	14.0%	2.9%				
 <i>Political Subdivision Employees</i>							
	1st Year Employment	2nd Year Employment	Ultimate				
<i>Male</i>							
Age 30	24.8%	21.0%	10.3%				
Age 40	21.0%	15.2%	7.2%				
Age 50	15.0%	12.8%	5.5%				
<i>Female</i>							
Age 30	24.8%	21.0%	11.8%				
Age 40	21.0%	15.2%	8.1%				
Age 50	15.0%	12.8%	5.9%				

ACTUARIAL DATA

SCHEDULE OF ACTIVE MEMBER VALUATION DATA

Valuation Year	Number	Annual Payroll In Thousands	Average Annual Pay	Average Annual Percentage Increase In Average Annual Pay
1985	140,744	\$ 2,377,928	\$ 16,895	6.51%
1987	147,779	2,800,035	18,947	5.90%
1989	153,664	3,215,050	20,922	5.08%
1991	158,820	3,636,495	22,897	4.61%
1993	166,443	3,943,079	23,690	1.72%
1995	175,584	4,580,041	26,085	4.93%
1997	180,637	4,940,816	27,352	2.40%
1999	189,592	5,473,772	28,871	2.74%
2001	195,946	5,997,047	30,606	2.96%
2003	200,597	6,504,434	32,425	2.93%

SCHEDULE OF RETIRED MEMBER VALUATION DATA

Valuation Year	Number	Annual Allowances In Thousands	Average Annual Allowances	Average Annual Percentage Increase In Average Allowances
1985	46,171	\$ 195,435	\$ 4,233	4.86%
1987	49,386	234,163	4,741	5.83%
1989	51,836	264,479	5,102	3.74%
1991	55,146	315,248	5,717	5.86%
1993	58,268	367,844	6,313	5.08%
1995	61,992	449,310	7,248	7.15%
1997	66,908	535,485	8,003	5.08%
1999	71,812	663,140	9,234	7.42%
2001	77,831	795,676	10,223	5.22%
2003	83,279	919,582	11,042	3.93%

SCHEDULE OF RETIRED MEMBER ACTIVITY

Expressed in Thousands

2-year period	Added to Rolls		Removed from Rolls		Rolls - End of Year		% Increase in Annual Allowances	Average Annual Allowances
	No.	Annual Allowances	No.	Annual Allowances	No.	Annual Allowances		
June 30								
1995	7,505	\$100,453	3,781	\$18,988	61,992	\$449,310	22.15%	\$7,248
1997	9,118	115,447	4,202	29,272	66,908	535,485	19.18%	8,003
1999	10,001	162,709	5,097	35,054	71,812	663,140	23.84%	9,234
2001	10,526	163,723	4,507	31,187	77,831	795,676	19.99%	10,223
2003	11,128	168,529	5,680	44,623	83,279	919,582	15.57%	11,042

Note: Timing differences exist between the data utilized for statistical information and that used for actuarial valuation purposes. Data is not available to present the required six year history on this schedule. Additional years will be added in future reports.

ACTUAL VS. RECOMMENDED CONTRIBUTION RATES

The Board adopted the contribution rates as recommended by the actuary.

ACTUARIAL BALANCE SHEET

ACTUARIAL BALANCE SHEET
as of July 1, 2003

ASSETS	State Employees, Teachers, Higher Ed. Employees Pension Plan (SETHEPP)	Political Subdivision Pension Plan (PSPP)	Total
Present assets creditable to			
Employer accumulation fund	\$ 19,191,061,582	\$ 2,914,374,745	\$ 22,105,436,327
Members' accumulation fund	2,908,190,130	691,154,611	3,599,344,741
Total present assets	<u>22,099,251,712</u>	<u>3,605,529,356</u>	<u>25,704,781,068</u>
Present value of prospective contributions payable to			
Employer accumulation fund			
Normal	3,004,425,125	967,109,743	3,971,534,868
Accrued liability	52,493,209	317,945,618	370,438,827
Total employer accumulation	<u>3,056,918,334</u>	<u>1,285,055,361</u>	<u>4,341,973,695</u>
Members' accumulation fund	<u>1,294,805,852</u>	<u>376,265,035</u>	<u>1,671,070,887</u>
Total prospective contributions	<u>4,351,724,186</u>	<u>1,661,320,396</u>	<u>6,013,044,582</u>
TOTAL ASSETS	<u>\$ 26,450,975,898</u>	<u>\$ 5,266,849,752</u>	<u>\$ 31,717,825,650</u>
LIABILITIES			
Present value of prospective benefits payable on account of			
Present retired members and beneficiaries	9,071,081,541	1,304,957,688	10,376,039,229
Present active members	16,960,751,035	3,851,255,879	20,812,006,914
Former members	419,143,322	110,636,185	529,779,507
TOTAL LIABILITIES	<u>\$ 26,450,975,898</u>	<u>\$ 5,266,849,752</u>	<u>\$ 31,717,825,650</u>

UNAUDITED

SHORT-TERM SOLVENCY TEST

<p>SHORT-TERMSOLVENCYTEST</p> <p>The financing objective of the Tennessee Consolidated Retirement System is to pay for the benefits provided by the plan through contributions that remain approximately level from year to year as a percentage of payroll, except that the strategy to fund the unfunded accrued liability is to make level-dollar payments over an established amortization period. A short-term solvency test is one means of checking a system’s progress under its funding program. In a short-term solvency test, the plan’s present assets are compared with: (1) active member contributions on deposit; (2) the liabilities for future benefits to present</p>	<p>retired lives; and (3) the liabilities for service already rendered by active members. In a system that has been following the approach of level percent of payroll financing for some time, the liabilities for active member contributions on deposit (liability 1) and the liabilities for future benefits to present retired lives (liability 2) should be fully covered by present assets. In addition, the liabilities for service already rendered by active members (liability 3) should be partially covered by the remainder of present assets. Generally, if the system has been using level cost financing, the funded portion of liability 3 will increase over time.</p>
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Dollar Amounts Expressed in Millions

Actuarial Valuation Year	Actuarial Accrued Liabilities for:			Valuation Assets	Portion of Actuarial Accrued Liabilities Covered by Assets		
	(1) Active Member Contributions	(2) Retirees and Beneficiaries	(3) Active Members (Employer Financed)		(1)	(2)	(3)
1993 SETHEEPP (1)	\$ 1,720.4	\$ 3,384.2	\$ 5,800.6	\$ 10,404.3	100%	100%	91%
PSPP (1)	321.6	426.1	696.1	1,400.9	100%	100%	94%
Total	\$ 2,042.0	\$ 3,810.3	\$ 6,496.7	\$ 11,805.2	100%	100%	92%
1995 SETHEEPP	\$ 1,995.7	\$ 3,958.4	\$ 6,731.6	\$ 12,319.2	100%	100%	95%
PSPP	384.8	534.2	830.1	1,707.8	100%	100%	95%
Total	\$ 2,380.5	\$ 4,492.6	\$ 7,561.7	\$ 14,027.0	100%	100%	95%
1997 SETHEEPP (2)	\$ 2,141.7	\$ 5,456.1	\$ 8,185.1	\$ 15,671.7	100%	100%	99%
PSPP (2)	426.4	743.6	1,117.9	2,226.9	100%	100%	95%
Total	\$ 2,568.1	\$ 6,199.7	\$ 9,303.0	\$ 17,898.6	100%	100%	98%
1999 SETHEEPP	\$ 2,396.6	\$ 6,401.8	\$ 9,621.8	\$ 18,327.1	100%	100%	99%
PSPP	501.4	877.1	1,512.4	2,690.8	100%	100%	87%
Total	\$ 2,898.0	\$ 7,278.9	\$ 11,134.2	\$ 21,017.9	100%	100%	97%
2001 SETHEEPP	\$ 2,638.6	\$ 7,837.6	\$ 10,366.1	\$ 20,761.0	100%	100%	99%
PSPP	592.0	1,104.2	1,831.9	3,188.0	100%	100%	81%
Total	\$ 3,230.6	\$ 8,941.8	\$ 12,198.0	\$ 23,949.0	100%	100%	97%
2003 SETHEEPP	\$ 2,908.2	\$ 9,071.1	\$ 10,172.5	\$ 22,099.3	100%	100%	99%
PSPP	691.1	1,304.9	1,927.4	3,605.5	100%	100%	84%
Total	\$ 3,599.3	\$ 10,376.0	\$ 12,099.9	\$ 25,704.8	100%	100%	97%

(1) Includes effect of five percent benefit improvement which became effective January 1, 1994.

(2) Includes effect of compound COLA and 3.6% indexing improvements.

SUMMARY OF ACCRUED AND UNFUNDED ACCRUED LIABILITIES

<p>The unfunded accrued liability represents the excess of the accrued actuarial liability over the actuarial value of assets. For funding purposes, the Board of Trustees of TCRS has adopted the frozen initial liability method.</p> <p>Under this method, the unfunded accrued liability is being funded by level-dollar contributions during an amortization period which ends in the year 2015. Also, actuarial gains and losses are absorbed in normal cost rather than as part of the unfunded liability. The statute governing TCRS allows the Board of Trustees to reestablish the unfunded accrued liability for actuarial gains and losses.</p> <p>For the July 1, 2003 actuarial valuation, the Board reestablished the unfunded accrued liability. In an</p>	<p>inflationary economy where the covered payroll continues to grow, the level-dollar amounts which are being contributed to fund the unfunded accrued liability will, if expressed as a percentage of payroll, continue to decrease.</p> <p>While concern is generally expressed regarding the dollar amount of the unfunded accrued liability, an analysis should also include the method being used to fund this liability as well as a review of this liability expressed as a percentage of active member payroll. The smaller the ratio of unfunded liabilities to the active member payroll, the stronger the system. A review of this ratio over a period of years will give an indication of whether the system is becoming financially stronger or weaker with respect to its unfunded liabilities.</p>
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SUMMARY OF ACCRUED AND UNFUNDED ACCRUED LIABILITIES

Dollar Amounts Expressed in Millions

Actuarial Valuation Year	Actuarial Accrued Liabilities (AAL)	Valuation Assets	Ratio Assets to AAL	Unfunded Actuarial Accrued Liabilities (UAAL)	Active Member Payroll	UAAL as a Percentage of Active Member Payroll
1993 (3)	12,349.0	11,805.2	96%	543.8	3,943.1	14%
1995	14,434.8	14,027.0	97%	407.8	4,580.0	9%
1997 (4)	18,070.8	17,898.6	99%	172.2 (1) (2)	4,940.8	3%
1999	21,311.1	21,017.9	99%	293.2 (1)	5,473.8	5%
2001	24,370.4	23,949.0	98%	421.4 (1) (2)	5,997.0	7%
2003	26,075.2	25,704.8	99%	370.4 (1)	6,504.4	6%

- Notes:
- (1) Unfunded accrued liability was reestablished.
 - (2) Includes adjustments for changes in actuarial assumptions.
 - (3) Includes effect of five percent benefit improvement effective January 1, 1994.
 - (4) Includes effect of compound COLA and 3.6% indexing improvement.

SELECTED ACTUARIAL FUNDING INFORMATION

SELECTED ACTUARIAL FUNDING INFORMATION

Actuarial Valuation Year	Earnings Assumption	Salary Assumptions	Unfunded Liability		State Amortization Period (3)
			SETHEPP	PSPP	
1993 (1)	8.0%	7.0%	\$ 500,933,773	42,897,901	10/22 (2)
1995	8.0%	7.0%	366,528,134	41,288,942	20
1997 (4)	7.5%	5.5%	111,172,072	61,012,975	18
1999	7.5%	5.5%	93,022,745	200,161,388	16
2001	7.5%	4.75% (5)	81,226,933	340,147,400	14
2003	7.5%	4.75% (5)	52,493,209	317,945,618	12

NOTES:

- (1) Includes effect of five percent benefit improvement which became effective January 1, 1994.
- (2) \$436.8 million is funded over 10 years and \$107 is funded over 22 years.
- (3) The amortization period varies among political subdivisions participating in TCRS with the maximum period limited to 30 years.
- (4) Includes effect of compound COLA and 3.6% indexing improvement.
- (5) Graded scale.

ANALYSIS OF FINANCIAL EXPERIENCE

GAIN AND LOSS ANALYSIS, JULY 1, 2003 VALUATION

	State and Higher Education	Teacher
Normal Cost		
Effective Employer Normal Cost Rate Pursuant to 2001 Valuation	7.30%	3.40%
Investment Results	2.71%	2.65%
Salary Increases: If there are smaller pay increases than assumed, the normal cost is reduced; if there are greater increases than assumed, the normal cost is increased.	(0.41%)	(0.48%)
New Entrants: Includes the effect where normal cost for new entrants since the previous valuation differs from the normal cost of the group.	0.34%	0.72%
Social Security Changes: More rapid increases in the Social Security wage base	(0.01%)	(0.03%)
Cost of Living Escalation: COLA in 2002 was 1.60%; 2003 was 2.40%.	(0.48%)	(0.44%)
Prior Service Purchases : Employee purchases of prior service credits result in liabilities to the plan that are not fully offset by related employee contributions	0.16%	0.09%
Contribution rate change delay	0.17%	(0.04%)
Change in actuarial assumptions (phase-in)	0.40%	-
Other	0.36%	(0.37%)
Effective Employer Normal Cost Rate Pursuant to 2003 Valuation	10.54%	5.50%

**RECONCILIATION OF UNFUNDED ACTUARIAL LIABILITIES
STATE EMPLOYEES, TEACHERS, AND HIGHER EDUCATION EMPLOYEES**

Unfunded Actuarial Liabilities at June 30, 2004	\$ 49,643,991
Interest Accrual Fiscal Year 2004-2005	3,249,843
Contributions Made toward Unfunded Actuarial Liabilities (Fiscal Year 2004-2005)	(6,312,752)
Unfunded Actuarial Liabilities at June 30, 2005	\$46,581,082

The remaining unfunded actuarial liabilities relates to two small closed plans for certain elected state and county officials. The two major plans for state employees and teachers do not have an unfunded liability.

PLAN SUMMARY

HISTORY AND ADMINISTRATION

The TCRS was established in 1972 by an Act of the Tennessee General Assembly. Seven existing retirement systems were consolidated to provide retirement, disability and death benefits to state employees, public school teachers, higher education employees and the employees of participating local governments. State laws governing the plan may be found in Chapters 34-37, 39 of Title 8, *Tennessee Code Annotated*. Amendments to the plan can only be made by legislation enacted by the General Assembly of the State of Tennessee.

An 18-member Board of Trustees has the responsibility to manage and oversee the operation of the consolidated system. The Board consists of nine ex-officio members from the executive, legislative, and judicial branches of state government and eight representatives of the active TCRS membership. Employee representation consists of three teachers, one from each grand division of the state, two state employees from departments other than those represented by ex-officio members, three representatives of local governments and one retired teacher representative. Local government representatives are appointed for two-year terms by each of the following organizations: the Tennessee County Services Association, the Tennessee Municipal League and the Tennessee County Officials Association. All employee representatives must be vested members of TCRS.

TCRS is administered by the Treasury Department under the legislative branch of state government. By state law, the State Treasurer serves as chairman of the Board of Trustees and as custodian of the funds of the system. The Director of the retirement system is appointed by the Treasurer and serves as the chief administrative officer of the plan.

The state is responsible for the pension cost of state employees and teachers; costs for the participation of local government employees are paid by political subdivisions. Administrative expenses are paid from employers' account balance. The operating budget is funded by local governments on a per member fee basis and by state government as part of the employer contribution rate.

MEMBERSHIP

Membership in the retirement system is a condition of employment for full-time state employees, K-12 teachers, higher education general employees and the employees of participating local governments. Membership is optional for part-time state employees and the part-time employees of political subdivisions which have authorized such coverage.

Interim teachers and part-time teachers have optional membership. The faculty employees of institutions of higher education may elect participation in either TCRS or an optional retirement program (ORP), a defined contribution plan for higher education faculty.

CONTRIBUTIONS

TCRS membership became noncontributory on July 1, 1981 for most state employees, teachers in state supported institutions of higher education and teachers employed in the Department of Education. At that time, the contributions, up to five percent of compensation payable to these employees, were assumed by the state, but this amount continued to be credited to the individual member's accounts from employer funds. State employees hired after July 1, 1981 join TCRS as noncontributory members with no funds credited to their individual accounts.

Participating political subdivisions may either adopt non-contributory retirement provisions or require employee contributions. The contribution rate for local government employees is five percent up to the social security wage base and 5.5 percent above that base, unless the employing government has authorized a level five percent rate. Public school teachers contribute at a rate of five percent of gross salary.

Individual accounts are maintained for all contributory members with interest credited annually at a rate of five percent. Since the TCRS is a defined benefit plan, benefits are based upon the member's average final compensation and years of creditable service. The member's account balance including interest accrued has no bearing on the monthly benefit amount payable at retirement. Account balances plus interest are fully refundable upon termination of service or death.

(continued)

PLAN SUMMARY (CONTINUED)

Contributory members are now covered by Section 414(h) of the Internal Revenue Code. Under this provision, retirement contributions are made on a tax-deferred basis, with income tax due only when contributions are returned to members as benefits or refunds. Political subdivisions may adopt the 414(h) provision for their employees.

The state also makes contributions on behalf of higher education faculty members who select membership in the ORP. These contributions are equal to 10 percent of salary up to social security wage base and 11 percent of any excess salary.

BENEFITS

TCRS provides three valuable benefits to its members: disability, death and service retirement. Disability benefits are available to qualified TCRS members who become totally disabled before meeting the requirements for service retirement. Two types of disability retirement are available: ordinary and accidental.

To qualify for ordinary disability, a member must have a minimum of five years of TCRS service credit. The ordinary disability benefit is equal to 90 percent of what the member would receive under service retirement. If a disabled retiree has less than 20 years of service credit, the service is projected to age 60 or 20 years, whichever comes first. When service is projected, the actual and projected service combined cannot exceed 20 years. If the member's actual service credit exceeds 20 years, the benefit is based on actual service only.

There is no minimum service requirement to qualify for an accidental disability benefit. However, the disability must be the result of a job-related accident that occurs without negligence on the part of the member, during the performance of duty. Prior to the onset of social security benefits, an accidental disability benefit is equal to 50 percent of the member's average final compensation (AFC). Once social security benefits begin, the accidental benefit is 33.3 percent of AFC. For members joining TCRS on or after July 1, 1997, accidental disability benefits are determined in the same manner as ordinary disability using the projection of service method. Disability benefits are increased by five percent for state employees, teachers and employees of participating political subdivisions which have authorized the five percent benefit improvement. The accidental benefit is adjusted if the

member's combined benefits from social security and/or workers' compensation exceed 75 percent of his AFC.

One of several death benefits may be payable to the designated beneficiary of an active member who dies prior to retirement. The type of death benefit payable will be determined by whether or not death occurred while in service, who is named as beneficiary, and the member's length of service.

A member may designate one or more persons, his estate, an institution, or any combination of such as his beneficiary. However, estates, institutions, and/or multiple beneficiaries are only eligible for a lump-sum refund of the member's accumulated contributions and interest unless one of the beneficiaries named is the surviving spouse. Other death benefits offered by TCRS include a 100 percent Joint and Surviving Spouse Annuity after 10 Years Service, a 100 percent Joint and Survivor Annuity for Any Beneficiary and a Line of Duty Benefit. Any beneficiary of a member who had 10 years of service and who is eligible for a lump-sum death benefit may elect a benefit to be paid over 10 years.

All members, with the exception of state judges, joining TCRS after 1976 enter the same membership group. The benefit formula for this group provides 1.5 percent of AFC computed over five years for each year of service credit. If a member's AFC exceeds the social security integration level (SSIL) applicable at retirement, the formula provides an additional 0.25 percent of the amount of the excess for each service year. These benefits are increased by five percent for state employees, teachers, and employees of participating political subdivisions which have authorized the five percent benefit improvement. State judges joining TCRS after September 1, 1990 become Group IV members.

Members become eligible for regular service retirement at age 60 and vested or at any age with 30 years. Vested members are eligible for reduced early retirement benefits when they have reached age 55 or have completed 25 years of service. Members joining TCRS after June 30, 1979 attain vesting rights after five years of service; the vesting period for members who joined prior to July 1, 1979 is four years. Five-year vesting and 25-year retirement are benefits that are optional to local governments. Otherwise, vesting for local governments is 10 years of service.

SERVICES FOR ACTIVE AND RETIRED MEMBERS

SERVICES FOR ACTIVE MEMBERS

TCRS provides a number of services for active members through its various sections.

Field Services

- ❖ TCRS staff is available to conduct employee presentations on all aspects of the retirement system.
- ❖ Employer seminars are conducted annually to educate retirement officers on legislation affecting TCRS.

Membership

- ❖ Comprehensive membership statements are provided to all members annually.
- ❖ Computer generated membership letters and membership pamphlets are mailed to all new members.
- ❖ Membership booklets are provided to all members periodically.
- ❖ The members' newsletter, *TCRS Report*, is sent to members semiannually.

Prior Service

- ❖ An automated calculation and eligibility system generates billings for members who wish to establish prior service.
- ❖ An installment program is available to purchase certain types of prior service.
- ❖ Prior Service may be purchased with a rollover from a tax-deferred 401(k) plan, 403(b) plan, 457 plan or an IRA.
- ❖ TCRS staff is available for personal counseling on an individual basis at their Nashville office.

Benefits

- ❖ Interactive benefit calculator via Internet.
- ❖ Computer generated benefit estimates are available for those members approaching retirement age.
- ❖ Annual regional employee benefit counseling workshops are available to educate potential retirees.
- ❖ TCRS staff is available for personal counseling on an individual basis at their Nashville office.
- ❖ Preretirement planning seminars, which explain all facets of post-career retirement planning, are provided for members.

SERVICES FOR RETIRED MEMBERS

A number of services are made available to TCRS retirees.

- ❖ A toll-free telephone line.
- ❖ Retiree identification cards.
- ❖ Semiannual retiree newsletter: *The Retiree Advisor*.
- ❖ Direct deposit service.
- ❖ Continuation of medical insurance.
- ❖ Medicare supplement coverage.
- ❖ Income tax information.
- ❖ Certification of monthly benefits.
- ❖ Certification of student discounts.
- ❖ Credit Union deductions.
- ❖ Tennessee State Employee Association deductions.
- ❖ Tennessee Retired Teachers Association deductions.

SAMPLE BENEFIT CALCULATIONS

TENNESSEE'S RETIREMENT PROGRAM, TCRS AND SOCIAL SECURITY BENEFITS
for Calendar Year 2005

Five-Year AFC*	Projected Annual Retirement Income	15 Years Service	% of AFC	20 Years Service	% of AFC	25 Years Service	% of AFC	30 Years Service	% of AFC	35 Years Service	% of AFC
\$15,000	TCRS	\$ 3,544		\$ 4,725		\$ 5,906		\$ 7,088		\$ 8,269	
	Social Security	8,976		8,976		8,976		8,976		8,976	
	Total	\$ 12,520	83.5%	\$ 13,701	91.3%	\$ 14,882	99.2%	\$ 16,064	107.1%	\$ 17,245	115.0%
\$20,000	TCRS	\$ 4,725		\$ 6,300		\$ 7,875		\$ 9,450		\$ 11,025	
	Social Security	10,560		10,560		10,560		10,560		10,560	
	Total	\$ 15,285	76.4%	\$ 16,860	84.3%	\$ 18,435	92.2%	\$ 20,010	100.1%	\$ 21,585	107.9%
\$25,000	TCRS	\$ 5,906		\$ 7,875		\$ 9,844		\$ 11,813		\$ 13,781	
	Social Security	12,144		12,144		12,144		12,144		12,144	
	Total	\$ 18,050	72.2%	\$ 20,019	80.1%	\$ 21,988	88.0%	\$ 23,957	95.8%	\$ 25,925	103.7%
\$30,000	TCRS	\$ 7,088		\$ 9,450		\$ 11,813		\$ 14,175		\$ 16,538	
	Social Security	13,728		13,728		13,728		13,728		13,728	
	Total	\$ 20,816	69.4%	\$ 23,178	77.3%	\$ 25,541	85.1%	\$ 27,903	93.0%	\$ 30,266	100.9%
\$35,000	TCRS	\$ 8,269		\$ 11,025		\$ 13,781		\$ 16,538		\$ 19,294	
	Social Security	15,312		15,312		15,312		15,312		15,312	
	Total	\$ 23,581	67.4%	\$ 26,337	75.2%	\$ 29,093	83.1%	\$ 31,850	91.0%	\$ 34,606	98.9%
\$40,000	TCRS	\$ 9,450		\$ 12,600		\$ 15,750		\$ 18,900		\$ 22,050	
	Social Security	16,896		16,896		16,896		16,896		16,896	
	Total	\$ 26,346	65.9%	\$ 29,496	73.7%	\$ 32,646	81.6%	\$ 35,796	89.5%	\$ 38,946	97.4%
\$45,000	TCRS	\$ 10,679		\$ 14,238		\$ 17,798		\$ 21,357		\$ 24,917	
	Social Security	18,384		18,384		18,384		18,384		18,384	
	Total	\$ 29,063	64.6%	\$ 32,622	72.5%	\$ 36,182	80.4%	\$ 39,741	88.3%	\$ 43,301	96.2%
\$50,000	TCRS	\$ 12,057		\$ 16,076		\$ 20,094		\$ 24,113		\$ 28,132	
	Social Security	19,068		19,068		19,068		19,068		19,068	
	Total	\$ 31,125	62.2%	\$ 35,144	70.3%	\$ 39,162	78.3%	\$ 43,181	86.4%	\$ 47,200	94.4%
\$55,000	TCRS	\$ 13,435		\$ 17,913		\$ 22,391		\$ 26,870		\$ 31,348	
	Social Security	19,716		19,716		19,716		19,716		19,716	
	Total	\$ 33,151	60.3%	\$ 37,629	68.4%	\$ 42,107	76.6%	\$ 46,586	84.7%	\$ 51,064	92.8%
\$60,000	TCRS	\$ 14,813		\$ 19,751		\$ 24,688		\$ 29,626		\$ 34,563	
	Social Security	20,292		20,292		20,292		20,292		20,292	
	Total	\$ 35,105	58.5%	\$ 40,043	66.7%	\$ 44,980	75.0%	\$ 49,918	83.2%	\$ 54,855	91.4%

* Average Final Compensation (AFC) is the average of the member's five highest consecutive years of salary.

This chart is based on a date of retirement in 2005. Social security benefits have been calculated by Bryan, Pendleton, Swats & McAllister, actuarial consultants for the TCRS, utilizing the following assumptions:

- (1) Retirement is taking place at age 65 in 2005;
- (2) The retiree has worked a full career (TCRS plus other employers, if necessary) of 35 years or more; and
- (3) Salary increases throughout the retiree's career have followed the same pattern as National Average Earnings.

The department's Internet benefits calculator allows members to receive an immediate estimate: www.treasury.state.tn.us/tcrs/

MAJOR LEGISLATIVE IMPROVEMENTS

<p>1972 Benefit formula improved from 1.12% of salary up to the SSIL to 1.5% of salary up to the SSIL.</p> <p>1973 Annual cost-of-living increase based on the CPI with a cap of 1.5% adopted for retirees.</p> <p>1974 Disability retirement eligibility requirement reduced from 10 years to 5 years of service.</p> <p>Minimum benefit increased from \$5.34 to \$7 per month per year of service.</p> <p>Maximum annual cost-of-living increase raised to 3%.</p> <p>Provision to increase retirees' benefits whenever the benefit formula is improved.</p> <p>Service credit authorized for unused accumulated sick leave.</p> <p>1976 Service retirement eligibility requirements reduced from age 65 or 35 years of service to age 60 or 30 years of service.</p> <p>Early retirement eligibility requirements reduced from age 60 or 30 years of service to age 55.</p> <p>1978 A bonus cost-of-living increase granted to retirees at a lump-sum cost of \$15.3 million.</p> <p>An optional retirement plan established for teachers in the Board of Regents system.</p> <p>1980 Death benefits for members dying in-service with 10 years of service improved by offering a 100% joint and survivor annuity of the member's accrued benefit for the spouse.</p> <p>1981 Noncontributory retirement for state employees and higher education employees adopted. Employees' contributions, up to 5%, were assumed by the state.</p> <p>1983 An actuarially reduced retirement benefit at any age with 25 years of service authorized.</p> <p>1984 Credit for out-of-state service for the purpose of determining retirement eligibility authorized.</p> <p>Retirement credit for armed conflict approved.</p> <p>Minimum benefit increased from \$7 to \$8 per month per year of service.</p> <p>Part-time employees permitted to participate in TCRS and members allowed to establish credit for previous part-time employment.</p>	<p>1985 \$22 million ad-hoc increase granted to retirees.</p> <p>Death benefits for spouse and children were provided when member's death is in the line of duty.</p> <p>1987 Service credit for half of peacetime military service made available.</p> <p>\$17 million ad-hoc increase granted to retirees.</p> <p>Retirement incentive for state employees.</p> <p>Section 414(h) of the IRC adopted, allowing employee contributions to be made on a tax-deferred basis.</p> <p>1990 Retirement incentive for state employees.</p> <p>1991 3.6% indexing of salaries for noncontributory employees extended one year. Each succeeding year up to 1997, the 3.6% indexing was extended. In 1997, it was extended indefinitely.</p> <p>1992 Minimum number of years required to qualify for retirement was reduced from 10 to 5 years.</p> <p>1993 Salary portability for service in different classifications authorized effective January 1, 1994.</p> <p>Benefit improvement up to 5% authorized.</p> <p>1994 Retirees permitted to work 100 days per year for a covered employer without loss of benefits.</p> <p>1997 Compounded COLA for retirees approved.</p> <p>Beginning date for armed conflict military service credit during the Vietnam Era was changed from August 4, 1964 to February 28, 1961.</p> <p>1998 Group 2 and 3 service requirements amended to permit service retirement with 30 years of service, regardless of age.</p> <p>Group 1 and Prior Class C benefit limitations increased to 80%.</p> <p>Mandatory retirement established with supplemental bridge benefit for all state public safety officers.</p> <p>1999 Group 1 benefit maximum increased to 90%.</p> <p>2000 Group 2 benefit maximum increased to 80%.</p> <p>2001 Line of Duty Death Benefits improved to guarantee a minimum \$50,000 death benefit.</p> <p>2005 Return to work statutes were reformed, including a temporary employment increase to 120 days.</p>
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"Hospital Duties"

Fold away all your bright-tinted dresses,
Turn the key on your jewels today.
And the wealth of your tendril-like tresses
Braid back in a serious way;
No more delicate gloves, no more laces,
No more trifling in boudoir or bower,
But come with your souls in your faces
To meet the stern wants of the hour....

Anonymous

The Battle of Shiloh, which took place
April 6-7, 1862, had 25,000 casualties.

"Gentle winds of springtime seem a sighing over a thousand new-made graves."
A Northern soldier writing about Shiloh

In 1862, Union soldiers
brought baseball to
Nashville, and they
played here in the
area of the Mall.

ated construction
Tennessee's
Union.
transferred
62.
its pattern
in Tennessee

SCHEDULES OF ACTIVE MEMBERS

SCHEDULE OF ACTIVE MEMBERS

by Service Credit

Years of Service	SETHEEPP			PSPP	Total
	State Employees	Teachers	Higher Education Employees	Political Subdivision Employees	
0 - 4	15,881	17,440	5,044	28,485	66,850
5 - 9	8,397	15,162	2,913	19,078	45,550
10 - 14	5,251	10,189	2,302	10,586	28,328
15 - 19	5,443	7,162	2,117	7,421	22,143
20 - 24	4,563	5,789	1,698	3,819	15,869
25 - 29	3,738	6,367	1,547	2,801	14,453
30 - 34	1,966	4,160	916	1,133	8,175
35 - 39	717	1,300	378	313	2,708
40 - 44	187	175	65	75	502
Over 44	62	47	22	26	157
Total	46,205	67,791	17,002	73,737	204,735

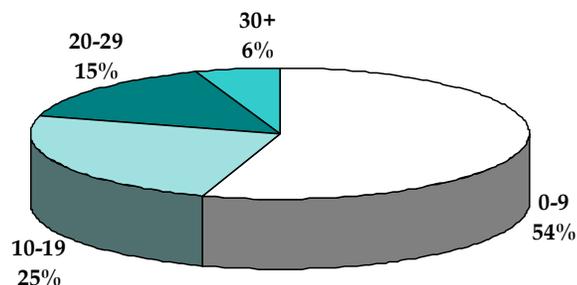
SCHEDULE OF ACTIVE MEMBERS

by Enrollment Date

Date of Membership	SETHEEPP			PSPP	Total
	State Employees	Teachers	Higher Education Employees	Political Subdivision Employees	
1940s	2	9	4	0	15
1950s	58	41	12	6	117
1960s	758	1,498	262	117	2,635
1970s	5,386	10,519	2,537	3,203	21,645
1980s	11,223	13,128	4,219	10,899	39,469
1990s	13,215	23,712	5,032	28,825	70,784
2000s	15,563	18,884	4,936	30,687	70,070
Total	46,205	67,791	17,002	73,737	204,735

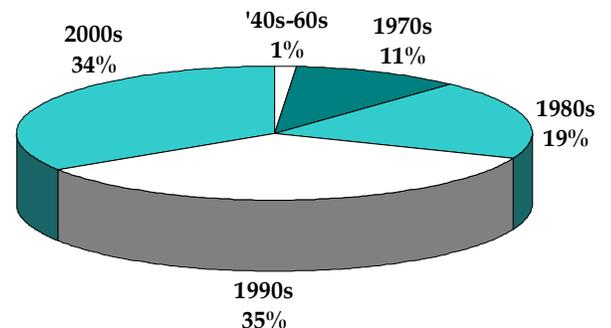
PERCENTAGE OF ACTIVE MEMBERS

by Service Credit



PERCENTAGE OF ACTIVE MEMBERS

by Enrollment Date



SCHEDULES OF ACTIVE MEMBERS

SCHEDULE OF ACTIVE MEMBERS

by Current Age

Current Age	SETHEEPP			PSPP	Total
	State Employees	Teachers	Higher Education Employees	Political Subdivision Employees	
Less than 20	62	7	8	73	150
20-29	4,944	8,850	1,273	6,739	21,806
30-39	8,743	17,292	2,659	15,678	44,372
40-49	12,909	16,277	4,793	22,315	56,294
50-54	7,784	11,402	2,954	10,791	32,931
55-59	6,806	9,900	2,758	9,253	28,717
60-64	3,329	3,331	1,659	5,458	13,777
65-69	1,121	582	633	2,177	4,513
Over 69	507	150	265	1,253	2,175
Total	46,205	67,791	17,002	73,737	204,735

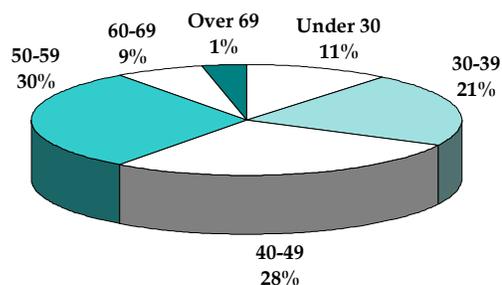
SCHEDULE OF ACTIVE MEMBERS

by Age at Enrollment

Age at Enrollment	SETHEEPP			PSPP	Total
	State Employees	Teachers	Higher Education Employees	Political Subdivision Employees	
Less than 20	1,619	119	312	1,147	3,197
20 - 24	9,602	23,659	2,837	9,135	45,233
25 - 29	9,669	16,604	3,307	11,092	40,672
30 - 34	6,960	9,015	2,889	11,958	30,822
35 - 39	5,874	7,235	2,658	12,334	28,101
40 - 44	4,677	5,351	2,048	10,635	22,711
45 - 49	3,570	3,316	1,457	7,448	15,791
50 - 54	2,386	1,694	913	5,068	10,061
55 - 59	1,357	661	415	2,976	5,409
60 - 64	371	109	116	1,249	1,845
65 - 69	97	22	38	512	669
Over 69	23	6	12	183	224
Total	46,205	67,791	17,002	73,737	204,735

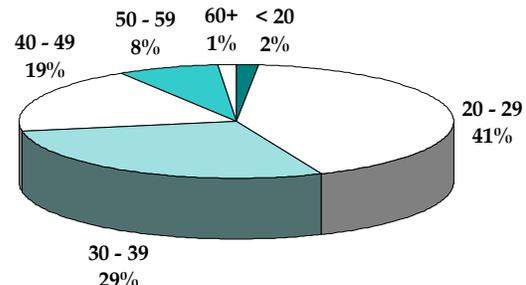
PERCENTAGE OF ACTIVE MEMBERS

by Current Age



PERCENTAGE OF ACTIVE MEMBERS

by Age at Enrollment



SCHEDULES OF ACTIVE MEMBERS

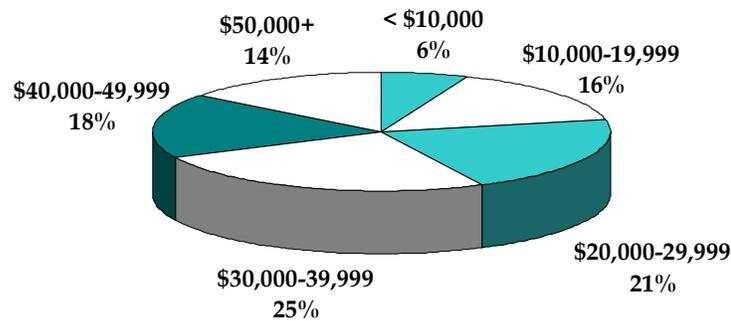
SCHEDULE OF ACTIVE MEMBERS

by Salary

Annual Salary	SETHEEPP			PSPP	Total
	State Employees	Teachers	Higher Education Employees	Political Subdivision Employees	
Less than \$10,000	2,866	266	809	8,458	12,399
\$10,000-19,999	5,308	1,063	2,351	23,447	32,169
\$20,000-29,999	14,352	3,257	5,458	20,207	43,274
\$30,000-39,999	11,286	23,989	3,355	12,550	51,180
\$40,000-49,999	6,141	23,263	1,762	5,060	36,226
\$50,000+	6,252	15,953	3,267	4,015	29,487
Total	46,205	67,791	17,002	73,737	204,735

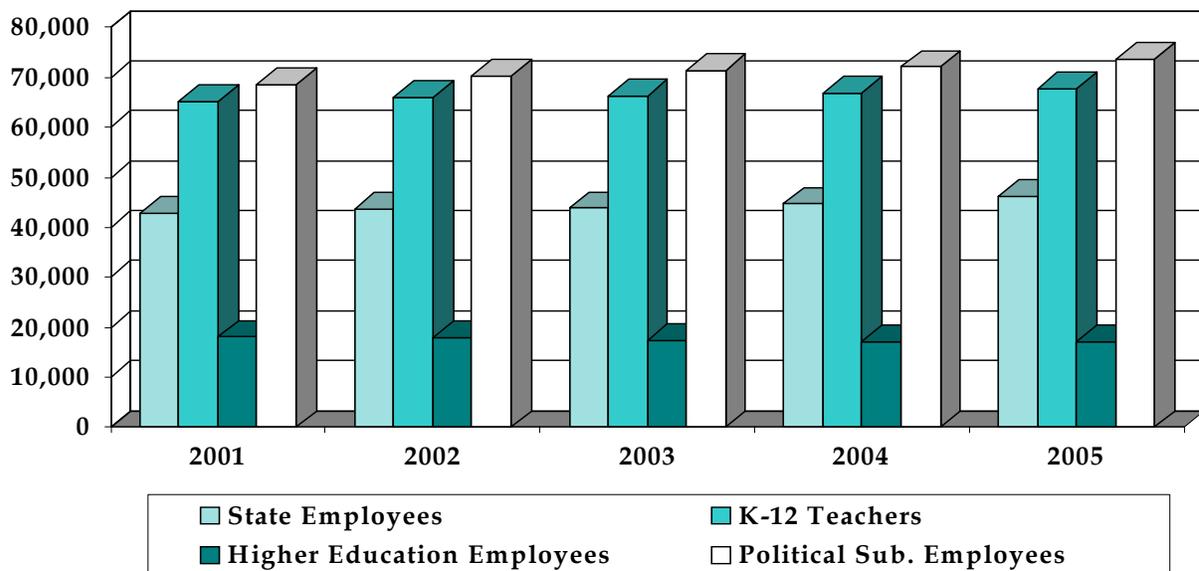
PERCENTAGE OF ACTIVE MEMBERS

by Salary



ACTIVE MEMBERS

Fiscal Years 2001-2005



SCHEDULES OF RETIRED MEMBERS

SCHEDULE OF RETIRED MEMBERS

by Type of Benefit Plan

Benefit Plan*	SETHEEPP			PSPP	Total
	State	Teachers	Higher Education	Political Subdivision	
	Employees		Employees	Employees	
Regular	11,371	19,524	5,910	16,392	53,197
Option I	1,689	1,513	1,292	1,831	6,325
Option II	810	749	535	637	2,731
Option III	2,148	2,359	1,090	1,917	7,514
Option IV	1,589	2,219	894	1,053	5,755
S.S. Leveling	1,444	3,172	366	1,130	6,112
Subtotal	19,051	29,536	10,087	22,960	81,634
Survivors	2,773	1,796	1,294	2,275	8,138
Total	21,824	31,332	11,381	25,235	89,772

- * Regular Maximum Plan - No Survivor Benefits
- * Option I 100% Joint and Survivor Annuity
- * Option II 50% Joint and Survivor Annuity
- * Option III 100% Joint and Survivor Annuity with Pop-up Feature
- * Option IV 50% Joint and Survivor Annuity with Pop-up Feature
- * S.S. Leveling Benefit Level Coordinated with Social Security

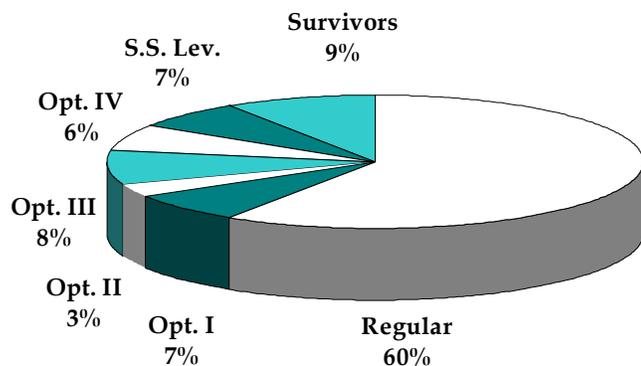
SCHEDULE OF RETIRED MEMBERS

by Type of Retirement

Type of Retirement	SETHEEPP			PSPP	Total
	State	Teachers	Higher Education	Political Subdivision	
	Employees		Employees	Employees	
Retirees:					
Service	15,130	24,687	7,962	17,806	65,585
Early	2,530	3,991	1,574	3,474	11,569
Disability	1,391	858	551	1,680	4,480
Total Retirees	19,051	29,536	10,087	22,960	81,634
Survivors	2,773	1,796	1,294	2,275	8,138
Total	21,824	31,332	11,381	25,235	89,772

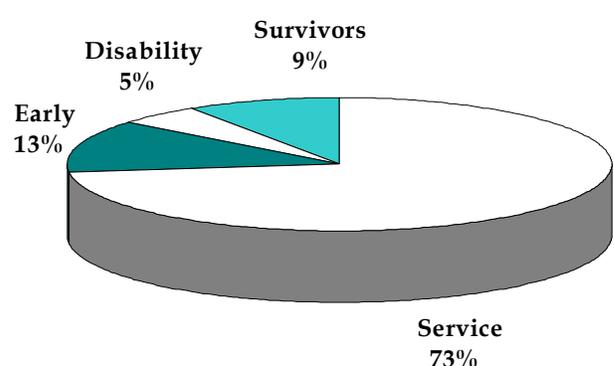
PERCENTAGE OF RETIRED MEMBERS

by Type of Benefit Plan



PERCENTAGE OF RETIRED MEMBERS

by Type of Retirement



SCHEDULES OF RETIRED MEMBERS

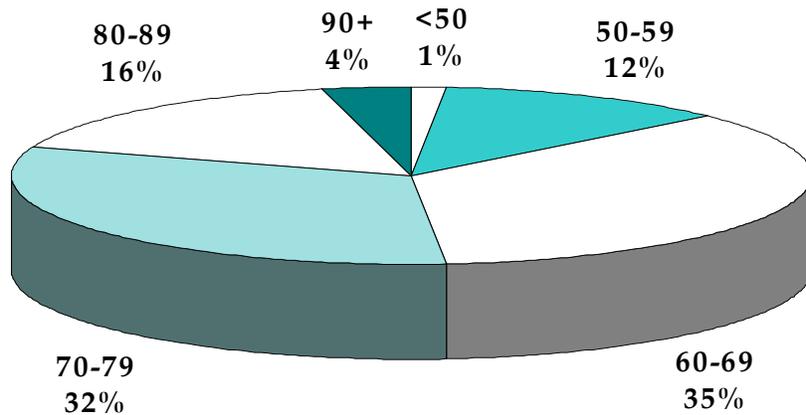
SCHEDULE OF RETIRED MEMBERS

by Current Age

Current Age	SETHEEPP			PSPP	Total
	State Employees	Teachers	Higher Education Employees	Political Subdivision Employees	
Under 40	108	68	36	72	284
40-44	110	58	38	87	293
45-49	244	110	99	182	635
50-54	657	745	228	576	2,206
55-59	2,100	3,912	770	1,762	8,544
60-64	3,436	5,459	1,662	3,686	14,243
65-69	4,102	5,554	2,280	5,440	17,376
70-74	3,825	4,753	2,205	5,050	15,833
75-79	3,143	4,058	1,845	3,647	12,693
80-84	2,246	2,694	1,316	2,591	8,847
85-89	1,265	2,080	653	1,472	5,470
90-94	484	1,299	207	550	2,540
95-99	95	466	36	114	711
Over 99	9	76	6	6	97
Total	21,824	31,332	11,381	25,235	89,772

PERCENTAGE OF TOTAL RETIRED MEMBERS

by Current Age



SCHEDULES OF RETIRED MEMBERS

SCHEDULE OF RETIRED MEMBERS

by Date of Retirement

Date of Retirement	SETHEEPP			PSPP	Total
	State Employees	Teachers	Higher Education Employees	Political Subdivision Employees	
1950s	1	14	0	2	17
1960s	29	139	7	4	179
1970s	1,096	2,676	405	1,118	5,295
1980s	4,129	6,524	2,169	4,583	17,405
1990s	9,512	11,586	5,241	10,491	36,830
2000s	7,057	10,393	3,559	9,037	30,046
Total	21,824	31,332	11,381	25,235	89,772

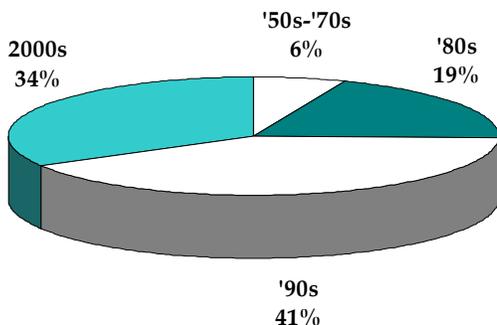
SCHEDULE OF RETIRED MEMBERS

by Service Credit at Retirement

Years of Service	SETHEEPP			PSPP	Total
	State Employees	Teachers	Higher Education Employees	Political Subdivision Employees	
Under 10	4,574	2,363	2,147	5,595	14,679
10-14	3,043	1,860	1,694	5,078	11,675
15-19	2,756	2,306	1,594	4,446	11,102
20-24	2,840	3,374	1,495	3,817	11,526
25-29	2,420	4,622	1,351	2,815	11,208
30-34	4,061	10,764	1,928	2,546	19,299
35-39	1,405	4,148	780	688	7,021
40-44	582	1,621	294	211	2,708
Over 44	143	274	98	39	554
Total	21,824	31,332	11,381	25,235	89,772

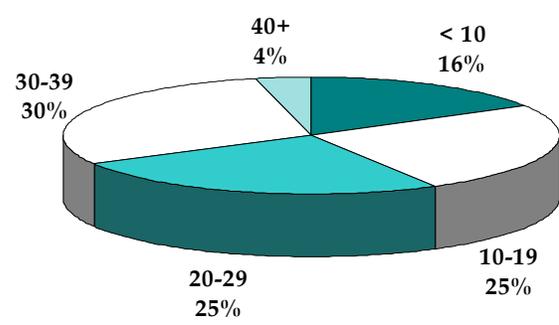
PERCENTAGE OF RETIRED MEMBERS

by Date of Retirement



PERCENTAGE OF RETIRED MEMBERS

by Service Credit at Retirement



RETIRED MEMBERS BY GEOGRAPHICAL DISTRIBUTION

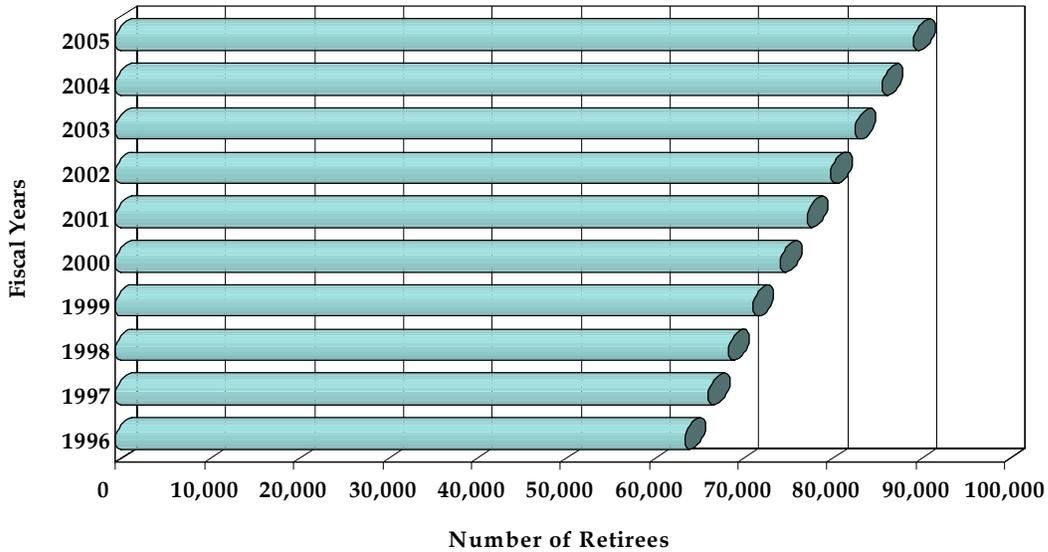
UNITED STATES				INTERNATIONAL COUNTRIES			
Alabama	440	Kentucky	405	North Dakota	2	Australia	1
Alaska	16	Louisiana	59	Ohio	105	Canada	8
Arizona	110	Maine	15	Oklahoma	47	England	2
Arkansas	279	Maryland	67	Oregon	31	France	1
California	143	Massachusetts	12	Pennsylvania	56	Germany	2
Colorado	55	Michigan	75	Rhode Island	2	Greece	2
Connecticut	5	Minnesota	18	South Carolina	163	Ireland	1
Delaware	10	Mississippi	796	South Dakota	6	Israel	1
Dist. of Columbia	9	Missouri	101	Tennessee	83,451	Japan	1
Florida	993	Montana	6	Texas	303	Kenya	1
Georgia	740	Nebraska	5	Utah	9	Mexico	2
Hawaii	12	Nevada	34	Vermont	7	Spain	1
Idaho	20	New Hampshire	20	Virginia	364	Total Foreign Countries	23
Illinois	91	New Jersey	15	Washington	47	US Virgin Islands	1
Indiana	81	New Mexico	28	West Virginia	22	Overseas Military Bases	11
Iowa	9	New York	42	Wisconsin	27	Total U.S.	89,737
Kansas	28	North Carolina	353	Wyoming	3	Total	89,772
				Total U.S.	89,737		

TENNESSEE

Anderson	1,262	Fentress	261	Lauderdale	550	Roane	1,074
Bedford	538	Franklin	610	Lawrence	616	Robertson	774
Benton	274	Gibson	902	Lewis	218	Rutherford	2,347
Bledsoe	326	Giles	429	Lincoln	488	Scott	393
Blount	2,106	Grainger	232	Loudon	598	Sequatchie	218
Bradley	1,104	Greene	1,514	McMinn	682	Sevier	784
Campbell	626	Grundy	250	McNairy	408	Shelby	9,469
Cannon	247	Hamblen	938	Macon	179	Smith	300
Carroll	486	Hamilton	4,131	Madison	1,904	Stewart	142
Carter	1,247	Hancock	69	Marion	364	Sullivan	2,635
Cheatham	532	Hardeman	739	Marshall	392	Sumner	1,759
Chester	317	Hardin	455	Maury	690	Tipton	580
Claiborne	540	Hawkins	752	Meigs	128	Trousdale	136
Clay	121	Haywood	452	Monroe	536	Unicoi	324
Cocke	461	Henderson	269	Montgomery	1,749	Union	235
Coffee	741	Henry	634	Moore	90	VanBuren	163
Crockett	252	Hickman	415	Morgan	486	Warren	612
Cumberland	702	Houston	77	Obion	652	Washington	2,255
Davidson	6,954	Humphreys	318	Overton	361	Wayne	257
Decatur	187	Jackson	178	Perry	205	Weakley	891
Dekalb	244	Jefferson	679	Pickett	100	White	472
Dickson	568	Johnson	276	Polk	182	Williamson	1,575
Dyer	418	Knox	5,505	Putnam	1,538	Wilson	1,372
Fayette	650	Lake	199	Rhea	381	Total Tennessee	83,451

**RETIRED MEMBERS ON PAYROLL
AND PRIOR SERVICE ESTABLISHED**

NUMBER OF RETIREES ON PAYROLL
Fiscal Years 1996-2005



PRIOR SERVICE ESTABLISHED
for the Year Ended June 30, 2005

Type of Service	Members	Years of Service	Payments
State:			
Backpayment	142	155	\$ 724,987
Military	134	294	16,096
Redeposit	140	620	1,260,208
Total	416	1,069	\$2,001,291
Teachers:			
Backpayment	136	174	\$1,051,679
Military	42	92	3,293
Redeposit	215	1,060	2,366,625
Total	393	1,326	\$3,421,597
Higher Education:			
Backpayment	200	271	\$ 294,578
Military	53	129	0
Redeposit	34	116	309,624
Total	287	516	\$ 604,202
Political Subdivisions:			
Backpayment	785	1,388	\$1,182,985
Military	165	358	23,914
Redeposit	85	466	773,696
Total	1,035	2,212	\$1,980,595
Totals by Category:			
Backpayment	1,263	1,988	\$3,254,229
Military	394	873	43,303
Redeposit	474	2,262	4,710,153
Total	2,131	5,123	\$8,007,685

TREASURY RETIREMENT INSTALLMENT PLAN

The Treasury Retirement Installment Plan, known as TRIP, was established in 1996 to be an alternative for members who have prior service to be established. Previously, prior service payments were required to be made in a lump sum payment. TRIP has allowed these members to establish their prior service by making monthly installment payments in the form of Automated Clearing House (ACH) withdrawals from a designated bank account. Prior service may be financed over a period not to exceed five years.

Examples of service types which are eligible to be included on TRIP are previously withdrawn service, peacetime military service, educational leave and enrollment service for new participating employers. When a member is billed for their prior service, a statement is generated showing a lump sum payment. In addition, TRIP information is given with regard to financing over 6 to 60 months. The member may elect to finance the entire amount or elect to make a down payment and finance the balance.

Annual statements are also generated as of the fiscal year ending June 30. Statements reflect the principle and interest payments made and remaining balance. The member may choose at any time to pay off the remaining balance.

TREASURY RETIREMENT INSTALLMENT PLAN
Payments Received for the Year Ended June 30, 2005

Type of Service	Members	Years of Service	Payments
State:			
Backpayment	9	27	\$ 24,807
Military	1	1	2,775
Redeposit	89	464	266,329
Total	99	492	\$ 293,911
Teachers:			
Backpayment	19	61	\$ 60,071
Military	0	0	0
Redeposit	175	879	663,285
Total	194	940	\$ 723,356
Higher Education:			
Backpayment	19	83	\$ 45,752
Military	0	0	0
Redeposit	12	54	24,520
Total	31	137	\$ 70,272
Political Subdivisions:			
Backpayment	29	185	\$ 66,985
Military	0	0	0
Redeposit	76	419	194,930
Total	105	604	\$ 261,915
Totals by Category:			
Backpayment	76	356	\$ 197,615
Military	1	1	2,775
Redeposit	352	1,816	1,149,064
Total	429	2,173	\$1,349,454

REFUND ACTIVITY AND POLITICAL SUBDIVISION PARTICIPATION**REFUND ACTIVITY**

For the Year Ended June 30	Number of Refunds Processed	Amount Refunded
1996	4,663	\$ 20,721,711
1997	4,632	23,833,152
1998	4,571	24,649,359
1999	4,874	25,634,380
2000	5,029	28,562,230
2001	4,771	28,517,803
2002	4,259	24,304,536
2003	4,540	26,631,386
2004	4,688	29,925,762
2005	4,724	30,815,699

The TCRS became noncontributory July 1, 1981 for state employees, higher education employees, and certain political subdivisions, resulting in fewer refunds for members withdrawing from the system.

POLITICAL SUBDIVISION PARTICIPATION*Schedule by Category*

Year Ended June 30	Number of Cities	Number of Counties	Miscellaneous Political Subdivisions	Total
1996	128	84	144	356
1997	134	84	156	374
1998	142	86	160	388
1999	147	87	170	404
2000	151	87	158	396
2001	156	87	161	404
2002	158	87	166	411
2003	160	88	170	418
2004	163	88	179	430
2005	169	88	187	444

HISTORICAL EMPLOYER CONTRIBUTION RATES

HISTORICAL EMPLOYER CONTRIBUTION RATES

Expressed as a Percentage of Salary

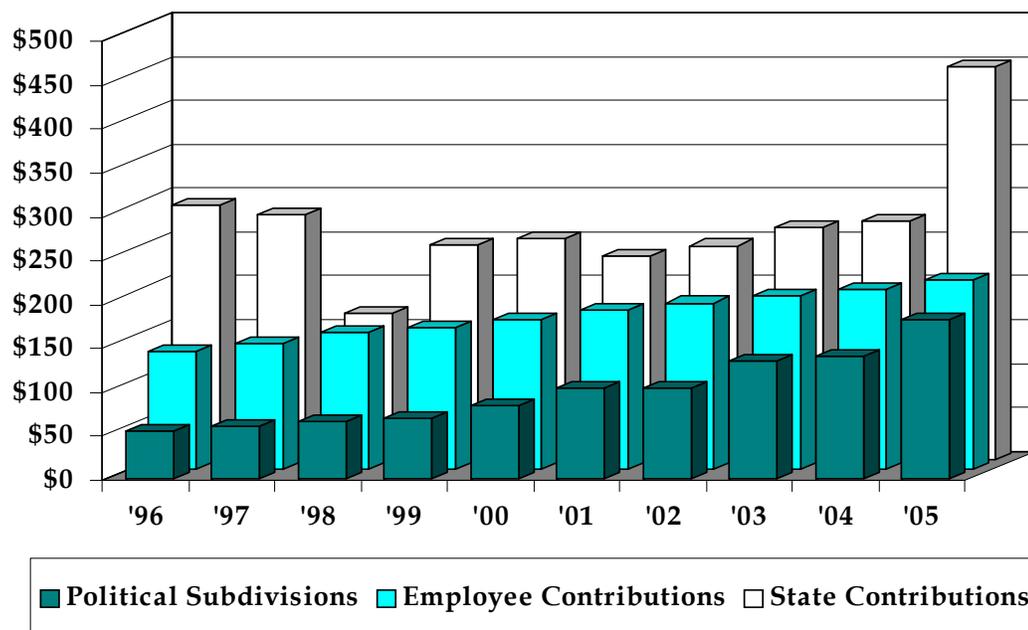
Year Ended June 30	State Employees	Teachers	Higher Education Employees Faculty	General
1996	6.33%	8.51%	6.33%	6.33%
1997	7.36	6.50	7.36	7.36
1998	3.65	3.89	3.65	3.65
1999	5.43	5.47	5.43	5.43
2000	5.43	5.47	5.43	5.43
2001	6.19	3.72	6.19	6.19
2002	6.19	3.72	6.19	6.19
2003	7.30	3.40	7.30	7.30
2004 (1)	7.29	3.39	7.29	7.29
2005	10.54	5.50	10.54	10.54

The employer contribution rates for political subdivisions are individually determined based on the biennial actuarial valuation of each political subdivision.

(1) As part of a statewide request for budget reductions, TCRS reduced the administrative component of the employer contribution rate by .01%.

RETIREMENT CONTRIBUTIONS

Fiscal Years 1996-2005



HISTORICAL FAIR VALUE

HISTORICAL FAIR VALUE

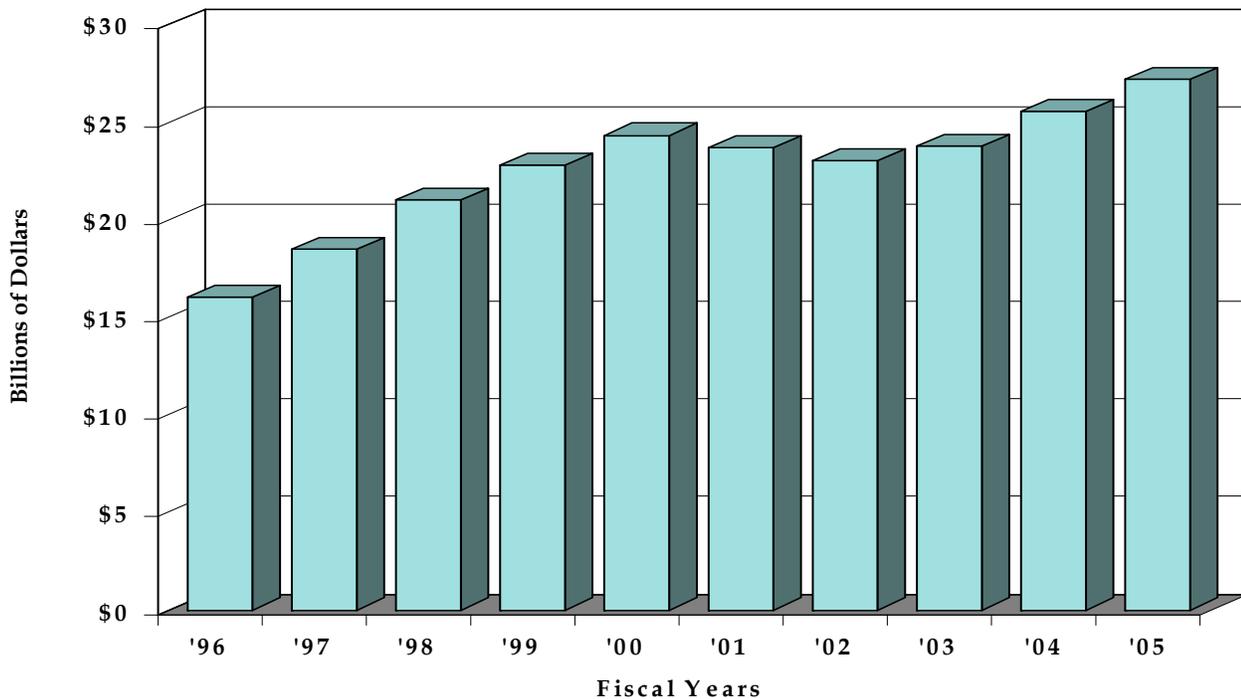
Fiscal Years 1996-2005

Expressed in Thousands

As of June 30	Fair Value	As of June 30	Fair Value
1996	\$16,072,177	2001	\$ 23,737,926
1997	18,519,341	2002	22,982,880
1998	21,057,487	2003	23,778,484
1999	22,797,512	2004	25,586,516
2000	24,337,679	2005	27,216,262

HISTORICAL FAIR VALUE

Fiscal Years 1996-2005



**ANALYSIS OF MEMBER AND EMPLOYER RESERVES
FOR THE YEAR ENDED JUNE 30, 2005**

MEMBER RESERVE FUND

The legislation which created the TCRS established two funds, the Member Reserve Fund and the Employer Reserve Fund, to account for the financial transactions of the pension plans. The Member Reserve Fund represents the accumulation of employee contributions plus interest.

	SETHEPP	PSPP	Total
<i>June 30, 2004 Member Reserve Fund</i>	\$ 3,059,174,900	\$ 746,905,134	\$ 3,806,080,034
Member Contributions	160,686,331	54,920,872	215,607,203
Employer Provided Contributions	24,124,768	11,366,055	35,490,823
Interest	142,602,230	35,227,316	177,829,546
Refunded Account Balances	(15,328,445)	(15,487,254)	(30,815,699)
Transfers to Employer Fund of Retiring Members' Account	<u>(203,422,429)</u>	<u>(37,492,991)</u>	<u>(240,915,420)</u>
<i>June 30, 2005 Member Reserve Fund</i>	<u><u>\$ 3,167,837,355</u></u>	<u><u>\$ 795,439,132</u></u>	<u><u>\$ 3,963,276,487</u></u>

EMPLOYER RESERVE FUND

The Employer Reserve Fund represents the accumulation of employer contributions, investment income and transfers from the Member Reserve Fund for retirees. Benefit payments and interest credited to members' accounts are reductions to the Employer Reserve Fund.

	SETHEPP	PSPP	Total
<i>June 30, 2004 Employer Reserve Fund</i>	\$ 18,835,505,045	\$ 2,944,931,173	\$ 21,780,436,218
Employer Contributions	448,153,153	181,096,392	629,249,545
Investment Income	1,579,232,000	271,135,215	1,850,367,215
Transfers from Retiring Members' Account	203,422,429	37,492,991	240,915,420
Employer Provided Contributions	(24,124,768)	(11,366,055)	(35,490,823)
Interest Credited to Members' Account	(142,602,230)	(35,227,316)	(177,829,546)
Lump-Sum Death Benefits	(3,731,252)	(1,180,113)	(4,911,365)
Retirement and Survivors Annuities	(887,527,677)	(136,477,559)	(1,024,005,236)
Administrative Expenses	<u>(3,008,497)</u>	<u>(2,737,533)</u>	<u>(5,746,030)</u>
<i>June 30, 2005 Employer Reserve Fund</i>	<u><u>\$ 20,005,318,203</u></u>	<u><u>\$ 3,247,667,195</u></u>	<u><u>\$ 23,252,985,398</u></u>

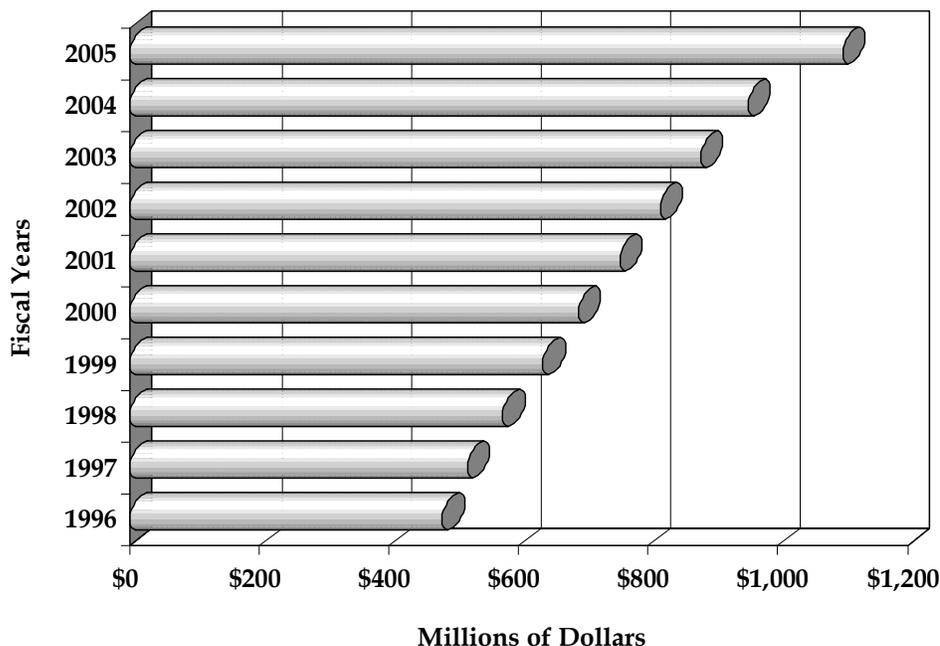
AVERAGE BENEFIT PAYMENTS SCHEDULE

AVERAGE BENEFIT PAYMENTS SCHEDULE
Fiscal Year of Retirement

	Years of Service Credit				
	10 - 14	15 - 19	20 - 24	25 - 29	30 or more
2000 Average Monthly Benefit	\$ 397	\$ 703	\$ 970	\$ 1,369	\$ 2,041
Number of Retirees	443	321	367	425	1,312
Average Final Salary	\$ 24,289	\$ 28,880	\$ 31,562	\$ 36,242	\$ 42,795
2001 Average Monthly Benefit	\$ 421	\$ 722	\$ 1,035	\$ 1,420	\$ 2,064
Number of Retirees	375	323	376	391	1,440
Average Final Salary	\$ 25,291	\$ 31,157	\$ 33,609	\$ 37,869	\$ 44,220
2002 Average Monthly Benefit	\$ 442	\$ 693	\$ 976	\$ 1,417	\$ 2,092
Number of Retirees	347	331	346	370	1,537
Average Final Salary	\$ 25,923	\$ 29,913	\$ 31,628	\$ 38,091	\$ 45,015
2003 Average Monthly Benefit	\$ 491	\$ 713	\$ 962	\$ 1,383	\$ 2,096
Number of Retirees	363	352	332	371	1,463
Average Final Salary	\$ 29,112	\$ 29,942	\$ 32,140	\$ 37,253	\$ 45,026
2004 Average Monthly Benefit	\$ 406	\$ 721	\$ 1,080	\$ 1,458	\$ 2,167
Number of Retirees	387	344	358	390	1,754
Average Final Salary	\$ 30,591	\$ 31,239	\$ 35,619	\$ 39,432	\$ 46,718
2005 Average Monthly Benefit	\$ 501	\$ 724	\$ 1,053	\$ 1,527	\$ 2,254
Number of Retirees	350	419	390	406	1,775
Average Final Salary	\$ 30,448	\$ 30,929	\$ 35,028	\$ 41,288	\$ 47,980

Note: This schedule represents the average monthly benefits under the maximum plan of members retiring with an unreduced service retirement benefit. It excludes members retiring with a reduced early retirement benefit or under disability.

ANNUAL BENEFIT PAYMENTS
Fiscal Years 1996-2005



SCHEDULES OF BENEFIT EXPENSES

SCHEDULES OF BENEFIT EXPENSES

Expressed in Thousands

Year Ending	Base Annuity	Disability Annuity	Survivor Annuity	Cost of Living	Lump-Sum Death Benefits	Total Benefits	Refunds	Total
SETHEEPP								
6/30/2000	\$ 450,919	\$ 15,089	\$ 28,839	\$ 106,542	\$ 2,658	\$ 604,047	\$ 15,474	\$ 619,521
6/30/2001	491,204	16,094	31,224	116,892	3,720	659,134	16,484	675,618
6/30/2002	528,471	17,405	33,518	129,918	2,225	711,537	12,689	724,226
6/30/2003	571,703	18,809	36,818	134,455	3,052	764,837	14,250	779,087
6/30/2004	617,659	20,341	40,022	145,767	3,149	826,938	15,305	842,243
6/30/2005	668,340	21,229	43,437	154,522	3,731	891,259	15,329	906,588
PSPP								
6/30/2000	\$ 69,164	\$ 2,315	\$ 4,423	\$ 11,933	\$ 852	\$ 88,687	\$ 13,088	\$ 101,775
6/30/2001	75,517	2,474	4,800	13,477	982	97,250	12,034	109,284
6/30/2002	82,084	2,704	5,206	15,417	1,143	106,554	11,616	118,170
6/30/2003	90,372	2,973	5,820	16,236	994	116,395	12,381	128,776
6/30/2004	98,680	3,250	6,394	17,860	1,329	127,513	14,621	142,134
6/30/2005	106,943	3,397	6,951	19,186	1,180	137,657	15,487	153,144

**SCHEDULES OF EXPENSES BY TYPE AND REVENUE BY SOURCE
FOR THE YEAR ENDED JUNE 30, 2005**

SCHEDULES OF EXPENSES BY TYPE

Expressed in Thousands

Year Ending	Benefit Payments	Administrative Expenses	Refunds	Total
SETHEEPP				
6/30/2000	\$604,047	\$2,363	\$15,474	\$621,884
6/30/2001	659,134	1,795	16,484	677,413
6/30/2002	711,537	2,714	12,689	726,940
6/30/2003	764,837	2,631	14,250	781,718
6/30/2004	826,938	2,935	15,305	845,178
6/30/2005	891,259	3,008	15,329	909,596

PSPP

6/30/2000	\$ 88,687	\$1,990	\$13,088	\$103,765
6/30/2001	97,250	1,683	12,034	110,967
6/30/2002	106,554	2,290	11,616	120,460
6/30/2003	116,395	2,425	12,381	131,201
6/30/2004	127,513	2,599	14,621	144,733
6/30/2005	137,657	2,738	15,487	155,882

SCHEDULES OF REVENUE BY SOURCE

Expressed in Thousands

Year Ending	Member Contributions	<u>Employer Contributions</u>		Investment Income (Loss)	Total
		Dollars	% of Annual Covered Payroll		
SETHEEPP					
6/30/2000	\$129,925	\$252,162	5.93%	\$1,533,113	\$1,915,200
6/30/2001	135,154	232,149	5.20%	(284,167)	83,136
6/30/2002	142,126	243,498	5.19%	(383,371)	2,253
6/30/2003	148,493	264,320	5.48%	959,110	1,371,923
6/30/2004	154,334	271,298	5.47%	1,870,972	2,296,604
6/30/2005	160,686	448,154	8.46%	1,579,232	2,188,072
PSPP					
6/30/2000	\$ 39,906	\$ 82,749	5.69%	\$ 227,961	\$ 350,616
6/30/2001	45,433	103,681	6.65%	(43,623)	105,491
6/30/2002	47,139	103,374	6.15%	(60,412)	90,101
6/30/2003	49,218	134,014	7.58%	153,368	336,600
6/30/2004	50,650	139,808	7.60%	310,881	501,339
6/30/2005	54,921	181,096	9.36%	271,135	507,152

INTRODUCTION TO POLITICAL SUBDIVISION PARTICIPATION

PARTICIPANTS

TCRS has established pension plans for four groups of public employees: state employees, higher education employees, teachers and the employees of governmental entities (political subdivisions). Employees of political subdivisions may participate in TCRS if the entity's governing body authorizes participation and accepts all liability associated with coverage for their employees.

Participation is subject to the approval of the Board of Trustees. As of June 30, 2005, 444 political subdivisions were participating in TCRS.

Participation as of June 30, 2005:

Cities	169
Counties	88
Utility Districts	46
Special School Districts	19
Joint Ventures	23
Housing Authorities	11
911 Emergency Communication Districts	36
Miscellaneous Authorities	52
Total	444

ADMINISTRATION

TCRS administers the pension plan for political subdivisions in accordance with state statute. Each employer is responsible for the pension cost for its employees. The cost is not shared with other political subdivisions nor with the state. A separate fund balance is maintained by the retirement system for each participating political subdivision and employer contribution rates are determined individually.

APPLICATION

To apply for TCRS participation, the chief governing body of the political subdivision must first pass a resolution authorizing an actuarial study to estimate the potential cost of participation. Once the governing body has had an opportunity to review the estimated pension cost and liability, a second resolution must then be passed in order to authorize TCRS participation. Political subdivisions electing TCRS coverage accept the liability for pension benefits to be accrued by their employees.

COVERAGE

A political subdivision is required to offer coverage under the same terms and conditions to all the employees of each of its departments and agencies.

Political subdivisions have the option of purchasing, or allowing their employees to purchase, retirement credit for service rendered prior to the employer's date of participation. The amount of prior service allowed may be limited.

Political subdivisions opting to join TCRS do so under the plan provisions that exist at the time of their participation. Subsequent legislative changes, however, are optional if they result in increased cost to the political subdivision. These optional improvements may be adopted by resolutions approved by the chief governing body.

**THE TCRS PROVIDES
THE ADMINISTRATION
OF A RETIREMENT
PROGRAM FOR 444
LOCAL GOVERNMENTS.**

OPTIONAL PROVISIONS FOR POLITICAL SUBDIVISIONS

<p>MEMBERSHIP</p> <ul style="list-style-type: none"> ❖ Optional membership for part-time employees ❖ Probationary period of up to six months during which the employees are not eligible for membership in TCRS and no contributions to TCRS are required of either the employees or the employer ❖ Reduce vesting requirement to qualify for retirement benefits from 10 years to five years <p>CONTRIBUTIONS</p> <ul style="list-style-type: none"> ❖ Employee contributions at a level five percent both below and above the social security wage base ❖ Exclusion of employee contributions from taxable income under 414(h) provisions of the Internal Revenue Code ❖ Noncontributory retirement plan ❖ Extension of 3.6 percent indexing feature for non-contributory members' salaries used in calculating the average final compensation component of a benefit calculation <p>CREDITABLE SERVICE</p> <ul style="list-style-type: none"> ❖ Credit for service credit lost as a result of advanced age ❖ Service credit for unused sick leave ❖ Service credit for military service during periods of armed conflict at no cost to the employee ❖ Service credit for periods of temporary disability during which the employee was receiving workers' compensation payments based on covered employment ❖ Service credit purchase for peacetime military service between October 15, 1940 and May 7, 1975 ❖ Purchase of service credit for probation period 	<p>SURVIVOR BENEFITS</p> <ul style="list-style-type: none"> ❖ 100 percent joint and survivor spouse death benefit for members with 10 years of service ❖ Provide inactive members with certain death and disability benefits ❖ 50 percent of 5 year average salary benefits for surviving spouse for members killed in the line of duty. <p>RETIREMENT BENEFITS</p> <ul style="list-style-type: none"> ❖ Provide current retirees and members a five percent increase in base retirement benefit ❖ The actuarial equivalent of an age 65 benefit for employees retiring after age 65 ❖ 25-year retirement with actuarially reduced benefits ❖ Minimum benefit level increase to \$8 per year of service ❖ Mandatory retirement with supplemental bridge benefit for public safety officers. <p>RETIRED MEMBERS</p> <ul style="list-style-type: none"> ❖ Exclusion of cost-of-living benefit increases at the date of participation for all employees or at a later date for new employees ❖ Inclusion of compounded cost-of-living adjustment (COLA) to current and future retirees of employers now providing a simple COLA or employers who previously elected not to provide a COLA. <p>MISCELLANEOUS</p> <ul style="list-style-type: none"> ❖ A participating entity may voluntarily withdraw from TCRS by submitting written notice one year in advance. At the time of withdrawal, TCRS membership ceases to be open to new employees. The political subdivision's retirement responsibility to current TCRS members remains, however, contribution obligations and benefit and service credit accruals continue.
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POLITICAL SUBDIVISION PARTICIPANTS

<p>911 EMERGENCY COMMUNICATION DISTRICTS</p> <p>Campbell County Carroll County Carter County Cheatham County Claiborne County Fayette County Fentress County Gibson County Grainger County Greene County Hamilton County Hamblen County Hardeman County Hawkins County Humphreys County Jefferson County Johnson County Lauderdale County Lawrence County Madison County Monroe County McNairy County Montgomery County Overton County Roane County Robertson County Rutherford County Sevier County Shelby County Sullivan County Tipton County Warren County Washington County Weakley County White County Wilson County</p>	<p>Byrdstown Camden Carthage Caryville Centerville Charleston Charlotte Church Hill Clarksville Cleveland Clifton Clinton Collegedale Collierville Collinwood Cookeville Coopertown Cornersville Cowan Crossville Dandridge Dayton Decaturville Dickson Dover Dunlap Dyer East Ridge Elizabethton Elkton Erin Erwin Estill Springs Etowah Fairview Fayetteville Forest Hills Friendship Friendsville Gainesboro Gatlinburg Gleason Goodlettsville Gordonsville Greenbrier Greenville Greenfield Harriman Hartsville Henderson Hendersonville Hohenwald Humboldt Huntland Jacksonboro Jackson Jamestown Jefferson City Johnson City Jonesborough</p>	<p>Kenton Kimball Kingsport Kingston Kingston Springs Lafayette Lafollette Lake City Lakeland Lakewood Lawrenceburg Lebanon Lenoir City* Linden Livingston Lobelville Lookout Mountain Loretto Loudon Luttrell Madisonville Martin Maryville Maury City Maynardville McEwen McKenzie McMinnville Middleton Milan Millersville Millington Morrison Morristown Moscow Mosheim Mountain City Mt. Carmel Mt. Juliet Munford Murfreesboro* New Johnsonville New Tazewell Newport Nolensville Norris Oak Ridge Oakland Obion Oliver Springs Paris Parsons Pikeville Pittman Center Pleasant View Portland Puryear Red Bank Ripley Rockwood</p>	<p>Rogersville* Rutledge Savannah Selmer Sevierville Signal Mountain Soddy Daisy Somerville South Carthage Sparta Spencer Spring Hill Spring City Springfield Sweetwater Tazewell Tellico Plains Townsend Trenton Tusculum Unicoi Union City Vonore Waynesboro Waverly Westmoreland White House White Pine Whiteville Whitwell Woodbury</p> <p>COUNTIES</p> <p>Anderson Bedford Benton Bledsoe Blount Bradley Campbell Cannon Carroll Carter Cheatham Chester Claiborne Clay Cocke Coffee Crockett Cumberland Decatur DeKalb Dickson Fayette Fentress Franklin Gibson Giles</p>	<p>Grainger Greene Grundy Hamblen Hamilton Hardeman Hardin Hawkins Haywood Henderson Henry Hickman Humphreys Jackson Jefferson Johnson Lake Lauderdale Lawrence Lewis* Lincoln Loudon Macon Madison Marion Marshall Maury McMinn McNairy Monroe Montgomery Moore* Morgan Obion Overton Perry Pickett Polk Putnam Rhea Roane Robertson Rutherford Scott Sequatchie Sevier Shelby* Smith Sullivan Sumner Tipton Trousdale Unicoi Union Van Buren Warren Washington Wayne Weakley White</p>	<p>Williamson Wilson</p> <p>HOUSING AUTHORITIES</p> <p>Bristol Clinton Cookeville Hartsville Hohenwald Lawrenceburg Maryville Memphis Morristown Rockwood Sweetwater</p> <p><i>*All departments not covered by TCRS.</i></p> <p><i>(continued)</i></p>
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**POLITICAL SUBDIVISION PARTICIPANTS
(CONTINUED)**

JOINT VENTURES

Argie Cooper Public Library
 Bradley-Cleveland Civil Defense
 Bradley-Cleveland Comm. Svc. Agency
 Clarksville/Montgomery Co. Public Lib.
 Clarksville/Montgomery Co. Reg.
 Planning Commission
 Cleveland/Bradley Community Center
 Committee
 Edward Gauche Fisher Public Library
 Fayetteville/Lincoln Co. Public Library
 Gorham/MacBane Public Library
 Jackson/Madison Co. Library
 Johnson City/Washington Co. EMS
 Kinser Park
 Lawrence Co. Library
 Linebaugh Public Library
 Morristown/Hamblen Co. Landfill
 Sevier Solid Waste
 Smyrna/Rutherford Co. Airport Auth.
 Tellico Area Svc. System
 Tri-City Airport Comm.
 Tri-County Vocational School
 W. G. Rhea Public Library
 Washington Co./Johnson City Animal
 Control Center
 Wilson Emergency Mgt. Agency

MISCELLANEOUS AGENCIES

Beech River Watershed
 Blount County Fire Protection Dist.
 Blount County Library
 Bristol/Kingsport/Sullivan Co.
 Industrial Commission Dist.
 Cookeville Reg. Medical Center Auth.
 County Officials Assoc. of Tenn.
 Delta Human Resource Agency
 Douglas Cherokee Economic Auth.
 East Tenn. Community Svc. Agency
 First Tenn. Dev. District
 First Tenn. Human Resource Agency
 Four Lake Reg. Industrial Dev. Auth.
 Greater Nashville Regional Council
 Hamilton Co. Comm. Svc. Agency
 Hardin County General Hospital
 Knox Co. Community Services Agency
 Mid-Cumberland Comm. Svc. Agency
 Melton Hill Regional Indust. Dev. Assoc.
 Newport/Locke Co. Economic Dev.
 Dist.
 Northeast Community Svc. Agency
 Northwest Tenn. Comm. Svc. Agency
 Sequatchie Valley Plan. & Dev. Dist.
 Shelby Co. Community Svc. Agency
 South Central Tenn. Community
 Services Agency
 South Central Tenn. Dev. Dist.
 South Central Tenn. Workforce Board
 Southeast Tenn. Comm. Svc. Agency

Southeast Tenn. Dev. District
 Southeast Tenn. Human Res. Agency
 Southwest Tenn. Comm. Svc. Agency
 Southwest Tenn. Dev. District
 Southwest Tenn. Human Res. Agency
 Tenn. Assoc. of Assessing Officers
 Tenn. Assoc. of County Mayors
 Tenn. Athletic Coaches Assoc.
 Tenn. Co. Commissioners Assoc.
 Tenn. Co. Highway Officials Assoc.
 Tenn. County Services Assoc.
 Tenn. Education Assoc.
 Tenn. Historical Society
 Tenn. Municipal Bond Fund
 Tenn. Municipal League
 Tenn. Mun. League Risk Mgt. Pool
 Tenn. Org. of School Superintendents
 Tenn. School Board Assoc.
 Tenn. Secondary Sch. Athletic Assoc.
 Tenn. Sheriffs Assoc.
 Tenn. State Employees Assoc.
 Tenn. Veterans Home Board
 Upper Cumberland Community Services
 Agency
 Upper East Tenn. Human Dev. Agency
 Workforce Solutions

SPECIAL SCHOOL DISTRICTS

Bradford
 Clinch Powell Education Coop.
 Elizabethton Board of Education
 Franklin
 Gibson County Schools District
 Hollow Rock-Bruceton
 Huntingdon
 Lebanon
 Little Tenn. Valley Education Coop.
 McKenzie
 Memphis
 Milan
 Oak Ridge Board of Education
 Oneida
 Paris
 South Carroll Special School District
 Trenton
 Union City Board of Education
 West Carroll County

UTILITY DISTRICTS

Alpha-Talbott
 Arthur Shawnee
 Big Creek
 Bloomingdale
 Bristol Electric System
 County Wide
 Crab Orchard
 Cumberland Utility District of Roane
 and Morgan Counties
 Double Springs
 Dyersburg Suburban
 East Fork
 East Side
 Fall Creek Falls
 First Carter County
 First Tipton County
 First Hawkins County
 Gladeville
 Glen Hills
 Greeneville Light & Power
 Hampton
 Hardeman-Fayette County
 Hendersonville
 Hixson
 Jackson County
 Johnson City Power Bd.
 Lake County
 Lincoln Co. Board of Public Utilities
 Middle Tennessee
 New Market
 North Utility District of Decatur and
 Benton Counties
 Northeast Henry County
 Oak Ridge
 Old Hickory
 Persia
 Poplar Grove
 Reelfoot Lake Regional
 Riceville
 Savannah Valley
 Sevier County
 Sylvia-Tennessee City Pond Water
 Sneedville
 Soddy Daisy-Falling Water
 Smith
 South Elizabethton
 Weakley Co. Municipal Electric
 Webb Creek

** All departments not covered by TCRS.*



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