City of San José

Comprehensive Annual Financial Report

For the Fiscal Year Ended June 30, 2007

Federated City Employees' Retirement System

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

A Pension Trust Fund of the City of San José, California

City of San José

Comprehensive Annual Financial Report

For the Fiscal Year Ended June 30, 2007

Federated City Employees' Retirement System

Edward F. Overton
Director

Department of Retirement Services

1737 North First Street, Suite 580

San José, California 95112-4505

408 392-6700 Phone

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www.sjretirement.com

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

A Pension Trust Fund of the City of San José, California

Board Chair Letter

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

September 13, 2007

The Honorable Mayor and City Council
Members of the Federated City Employees' Retirement System
City of San José
San José, California

Dear Mayor, Council Members and Plan Members:

On behalf of the members of the Board of Administration, I am pleased to present the Federated City Employees' Retirement System's ("the System") Comprehensive Annual Financial Report ("CAFR") for the fiscal year ended June 30, 2007. Some significant events worthy of note during this fiscal year were as follows:

- The System earned a time-weighted rate of return of 16.22% on investments, compared to 15.69% for its benchmark and 16.08% for the Trust Universe Comparison Service Public Fund Median. The System has earned an annualized return of 9.69% since the performance measurement inception date of December 31, 1993. The fair value of the System's investments increased from $1,624,456,000 to $1,860,643,000, net of pending purchases and sales, and excluding securities lending collateral (see Investment Summary on page 65).
- The System continued to make enhancements to the member services website during the fiscal year 2006-07. A Pilot Program for online open enrollment for members that were not Medicare eligible was implemented. The document imaging and retrieval system was also enhanced to include Board packets. All paper documents in the Board packets are now stored and retrievable in the System's pension administration system.
- The Board accepted Gabriel, Roeder, Smith, & Company's (GRS) special study report on Actuarial Valuation of Retirement Health Benefits as of June 30, 2006 (GASB 43/45).
- The System implemented the deduction for Allstate insurance whereby Retirees are able to purchase cancer insurance for the first time. This insurance pays benefits for non-medical cancer related expenses that health insurance might not cover.
- The Board continued to rebalance the portfolio based on the Asset Liability Modeling Study that was completed in fiscal year 2001-02.

The Board believes that the professional services rendered by the staff, the auditors, investment counselors, the actuarial consultants, and the Fund performance evaluators have produced a sound fund capable of continued growth. The Board of Administration and its staff are available to provide additional information when requested.

Sincerely,

David Busse
Chair, Board of Administration

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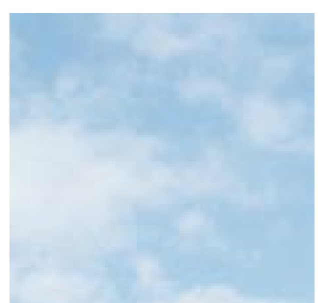
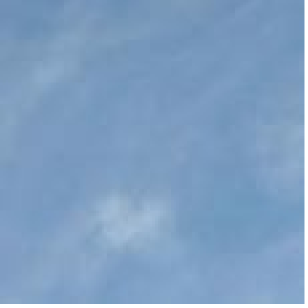


San José Federated City Employees' Retirement System

Comprehensive Annual Financial Report 2006 – 2007



Introductory Section

Letter of Transmittal

September 6, 2007

City of San José
Department of Retirement Services
Board of Administration
Federated City Employees' Retirement System
1737 North First Street, Suite 580
San José, CA 95112

Dear Board Members:

I am pleased to present the Comprehensive Annual Financial Report (CAFR) of the Federated City Employees' Retirement System (the System) for the fiscal year ended June 30, 2007. Responsibility for both the accuracy of the data, and the completeness and fairness of the presentation, rests with the System's management. Macias Gini & O'Connell LLP, the System's independent auditor, has audited the accompanying financial statements. Management believes that internal control is adequate and the accompanying statements, schedules and tables are fairly presented and free from material misstatement.

The System was established in 1941 and switched to the CAFR format for the fiscal year ended June 30, 2000. Information contained in this report is designed to provide a complete and accurate financial review of the year's operations. I am proud to report that last year's CAFR was awarded the Certificate of Achievement for Excellence in Financial Reporting from the Government Finance Officers Association. I encourage you to review the narrative introduction, overview and analysis located in Management's Discussion and Analysis beginning on page 12.

I trust that you and the members of the System will find this CAFR helpful in understanding the System; a plan that continues to maintain a strong and positive financial future.

Certificate of Achievement

The Government Finance Officers Association of the United States and Canada ("GFOA") awarded a Certificate of Achievement for Excellence in Financial Reporting to the System for its CAFR for the fiscal year ended June 30, 2006. The Certificate of Achievement is a prestigious national award recognizing conformance with the highest standards for preparation of state and local government financial reports.

To be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized CAFR, whose contents meet or exceed program standards. This report must satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid only for one year. The System first received the certificate for its fiscal year ended June 30, 2000 CAFR with its first application. We believe our current report continues to conform to the Certificate of Achievement Program Requirements, and we are submitting it to GFOA to determine its eligibility for another certificate.

The CAFR was prepared to conform to the principles of governmental accounting and reporting set forth by the Governmental Accounting Standards Board. Transactions of the System are reported on the accrual basis of accounting. Sufficient internal accounting controls exist to provide reasonable assurance regarding the safekeeping of assets and fair presentation of the financial statements and supporting schedules.

Major Initiatives

The System continued to make enhancements to the member services website during the fiscal year 2006-07. A Pilot Program for online open enrollment for members that are not Medicare eligible was implemented. The Document Imaging and Retrieval System was enhanced to include Board packets. All paper documents in the Board packets are now stored and retrievable in the System's pension administration system.

The Board accepted Gabriel, Roeder, Smith, & Company's (GRS) special study report on Actuarial Valuation of Retirement Health Benefits as of 30 June 2006 (GASB 43/45).

The System implemented the deduction of Allstate insurance whereby Retirees were able to purchase cancer insurance for the first time. This insurance pays benefits for non-medical cancer related expenses that health insurance might not cover.

Changes in System Membership

System membership changes for the defined benefit pension plan for fiscal year 2006-07 were as follows:

	2007	*2006*	*Increase*	*Change*
Active Members*	4,673	4,524	149	3.29%
Retired Members	2,315	2,206	108	4.9%
Survivors**	434	415	20	4.82%
TOTAL	**7, 422**	**7,145**	**277**	**3.88%**

**Active members include deferred vested members, members who have left City service but remain a member of the System.*

***Survivor total includes ex-spouses.*

Letter of Transmittal *Continued*

Financial and Economic Summary

Maintaining a long-term perspective is important when dealing with retirement assets. The annualized return since inception was 9.69%, which is ahead of the actuarial assumption rate of 8.25%. The fair value of the System's investments increased from $1,624,456,000 to $1,860,643,000, net of pending purchases and sales, excluding securities lending collateral (see Investment Summary on page 65).

The fiscal year ending June 30, 2007 marked a slowdown within the US economy as oil prices continued to rise while the housing market cooled significantly. The Consumer Price Index eased slightly on a year-over-year basis with a 2.7% increase. Tighter lending standards and higher mortgage rates have kept home sales low and inventory levels at record highs. The Fed left short-term interest rates unchanged at 5.25% during the year ending 6/30/07. The System's investment consultant, The Northern Trust Company, believes that the asset allocation strategy followed by the System's Board has benefited the plan's long-term return. The System is well structured to meet its investment objectives as defined in the Investment Policy Statement.

Investment Summary

The Board of Administration has exclusive control of all investments of the System and is responsible for the establishment of investment objectives, strategies and policies. Members of the Board serve in a fiduciary capacity and must discharge their duties with respect to the System and the investment portfolio solely in the interest of, and for the exclusive purposes of providing benefits to, members of the System and defraying the reasonable cost of administration.

For the fiscal year ended June 30, 2007, the time-weighted rate of return for the System was 16.22% versus the Benchmark return of 15.69%, which placed the System's total return in the second quartile of the Trust Universe Comparison Service ("TUCS") Public Fund and in the third quartile of the TUCS Master Trust Universe. Over long term periods, the portfolio has earned total annualized returns of 11.74% over the past three years and 11.78% over the past five years, and ranked in the 51st and the 26th percentiles, respectively, of the TUCS Public Fund Universe.

Funding

The System's funding objective is to meet long-term benefit obligations through contributions and investment income. As of June 30, 2005, the funding ratio of the System was approximately 80.9%. A six-year history of the System's funding progress is presented on page 37. The net increase in System assets for fiscal year 2006-07 was $239,042,000. Details of the components of this increase are included in the Statement of Changes in Plan Net Assets on page 22.

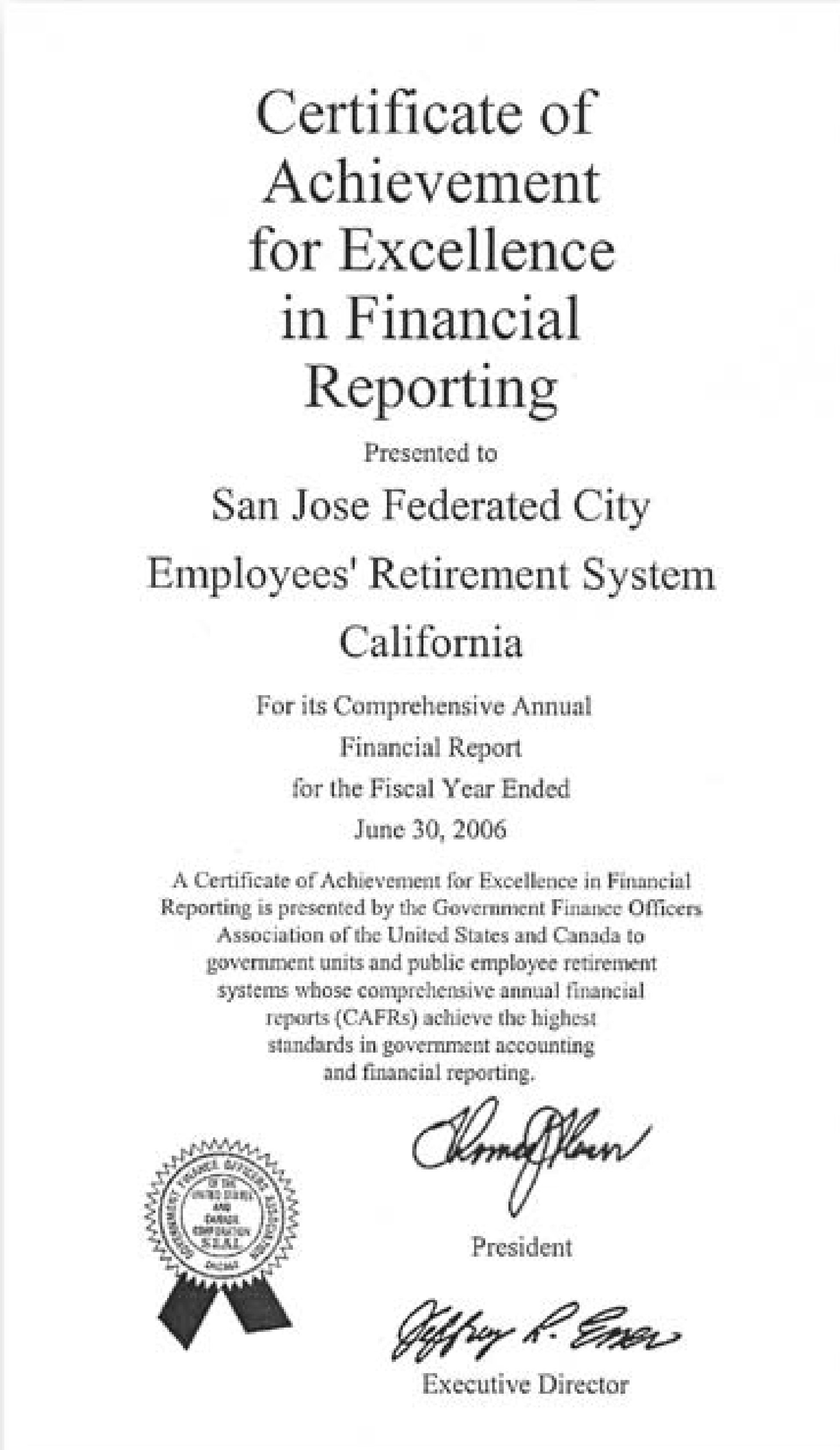
Conclusion

I would like to take this opportunity to thank the members of the System for their confidence in the plan management during the past year. I also want to express my thanks to the Board of Administration for its dedicated effort in supporting the staff through this past year. I thank the consultants and staff for their commitment to the System and for their diligent work to assure the System's continued successful operation.

Respectfully Submitted,

Edward F. Overton
Director, Retirement Services

Certificate of Achievement for Excellence in Financial Reporting



Certificate of Achievement for Excellence in Financial Reporting

Presented to

San Jose Federated City Employees' Retirement System California

For its Comprehensive Annual Financial Report for the Fiscal Year Ended June 30, 2006

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.

President

Executive Director

Board of Administration, Administration, and Outside Consultants

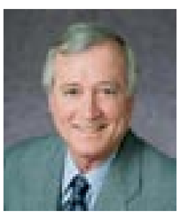
BOARD OF ADMINISTRATION

The Retirement System is administered by a seven-member Board of Administration composed of two City Council members, a member from the Civil Service Commission, two City employees elected by members of the system, a Retiree Representative, and a public member who is not connected with the City and has significant banking or investment experience selected by the four Board members and approved by the City Council. The Board is appointed by the City Council and serves in accordance with Section 2.08.300 of the San Jose Municipal Code.

As of June 30, 2007, the members of the Board were as follows:

DAVID BUSSE, CHAIRMAN
Civil Service Commission member appointed in February 2003. His current term expires December 1, 2010.

WILLAIM A. THOMAS, VICE CHAIRMAN
Retired Plan member appointed in August 2001. His current term expires November 30, 2008.



TIMOTHY CALLAHAN
Employee Representative elected to the Board in November 2005. His current term expires November 30, 2009.

PETE CONSTANT
City Council member appointed to the Board in January 2007.

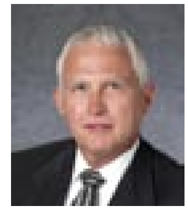
JEFFREY PERKINS
Public member appointed to the Board in June 1996. His current term expires November 30, 2010.

MIKE YOSHIMOTO
Employee Representative appointed to the Board in December 1999. His current term expires November 30, 2007.

FORREST WILLIAMS
City Council member appointed to the Board in August 2001.

ADMINISTRATION

EDWARD F. OVERTON
DIRECTOR, RETIREMENT SERVICES



THOMAS J. WEBSTER
DEPUTY DIRECTOR

OUTSIDE CONSULTANTS

ACTUARY
Gabriel, Roeder, Smith & Company
Denver, CO

ATTORNEY, BOARD
Saltzman & Johnson
San Francisco, CA

ATTORNEY, REAL ESTATE
Bingham McCutchen, LLP
East Palo Alto, CA

AUDITOR
Macias Gini & O'Connell LLP
Walnut Creek, CA

A list of Investment Professionals begins on page 53 of the Investment Section of this report.

STANDING PUBLIC MEETINGS

Board Meetings: Second Thursday of the Month, 8:30 AM

Investment Committee: Quarterly

Investment Committee of the Whole: Quarterly

Real Estate Committee: Ad Hoc

Agendas for all public meetings are posted on the bulletin board at City Hall and on the department's website at *http://sjretirement.com/FED/Meetings/Agendas.asp* or they can be obtained from the retirement office at 1737 North First Street, Suite 580, San Jose, CA 95112-4505. Meeting times and locations are subject to change; please call our office at (408) 392-6700 for current information.

Department of Retirement Services Organizational Chart

- **EDWARD F. OVERTON**, *Director*, 408 392-6703
  - **(VACANT)**, *Deputy Director*, *Chief Financial Officer*
    - **DONNA BUSSE**, *Investment Officer*, 408 392-6709
      - **RONALD R. KUMAR**, *Financial Analyst*, 408 392-6708
      - **UDAYA RAJBHANDARI**, *Financial Analyst*, 408 392-6717
      - **JUDY POWELL**, *Analyst*, 408 392-6716
      - **CRISTIN JAMES**, *Staff Specialist*, 408 392-6729
    - **COLLEEN HY**, *Senior Accountant*, 408 392-6719
      - **SUSAN PERREIRA**, *Accountant*, 408 392-6730
      - **HOA LANG**, *Accounting Technician*, 408 392-6721
      - **CION GARCIA**, *Senior Account Clerk*, 408 392-6730
      - **SELINA ORDAZ**, *Account Clerk*, 408 392-6722
  - **THOMAS J. WEBSTER**, *Deputy Director*, *Chief Operations Officer*, 408 392-6704
    - **DEBBI WARKENTIN**, *Administrative Assistant*, 408 392-6723
      - **TAMASHA JOHNSON**, *Secretary*, 408 392-6724
      - **ANDREA OGANA**, *Office Specialist*, 408 392-6700
      - **ROBIN JACQUES**, *Office Specialist*, 408 392-6700
    - **BARBARA HAYMAN**, *Information Systems Analyst*, 408 392-6710
      - **MAY CHEUNG**, *Systems Analyst*, 408 392-6711
      - **GINA BILLINGS**, *Network Technician II*, 408 392-6705
    - **ROGER PICKLER**, *Support Services Supervisor*, 408 392-6707
      - **TONI JOHNSON**, *Senior Analyst*, Pension Benefits, 408 392-6713
        - **AMANDA RAMOS**, *Analyst*, 408 392-6706
        - **MARIA LOERA**, *Analyst*, 408 392-6714
        - **MIKE PRIBULA**, *Analyst*, 408 392-6715
        - **(VACANT)**, *Staff Technician*, 408 392-6718
      - **CAROL BERMILLO**, *Analyst*, Health Benefits, 408 392-6720
      - **KARIN CARMICHAEL**, *Analyst*, Education/Training, 408 392-6712
        - **LINDA BROGAN**, *Staff Technician*, 408 392-6728

Department of Retirement Services
1737 North First Street, Suite 580
San Jose, CA 95112-4505
408 392-6700 Phone
800 732-6477 Phone
408 392-6732 Fax
www.sjretirement.com

Summary of the Principal System Provisions

MEMBERSHIP

Mandatory for all full-time non-safety employees.

MEMBER CONTRIBUTION

All members contribute 7.58% of base salary.

CITY'S CONTRIBUTION

The City contributes 21.98% of the base salary. The financing is designed to provide reserves sufficient to meet the accrued and accruing liabilities under the prescribed benefit schedule. (Rates are reviewed following each actuarial survey.)

RETIREMENT

Members may retire at age 55 with five or more years of service or at any age with 30 years of service.

RETIREMENT ANNUITY

The retirement annuity payable is the Final Average Salary multiplied by 2.5% per year of service (Maximum Benefit: 75% of the Final Average Salary).

FINAL AVERAGE SALARY

The average monthly salary for the highest twelve (12) consecutive months.

DISABILITY RETIREMENT

Non-Service-Connected

A non-service-connected disability annuity is available to members with five (5) or more years of service if the disability is permanent and prevents the member from performing any work in his/her present classification. The base non-service connected disability annuity is the greater of 40% of the Final Average Salary or the earned retirement allowance (Final Average Salary x 2.5% x Number of Years of Service). The annuity will be reduced by .5% for each year of age under 55.

For those entering the system September 1, 1998 or later, the calculation is as follows:

20% of Final Average Salary for 6 years of service;
add 2% for each year of service in excess of 6 years but less than 16 years;
add 2.5% for each year of service in excess of 16 years of service.

Service-Connected

A service-connected disability is available if the disability is permanent and directly due to and caused by actual performance of employment within the City. The minimum service-connected disability annuity is 40% of the final average salary. There is no minimum service requirement for a service-connected disability nor reduction factor due to age. The disability benefit is offset by certain workers' compensation payments. If a member has more than 16 years of service with the City of San Jose, they will also receive 2.5% of the Final Average Salary for each year in excess of 16 in addition to the 40% benefit for a Service-Connected Disability. (Maximum Benefit: 75% of the Final Average Salary)

TERMINATION BENEFITS

Upon termination, the member will be paid all of his or her accumulated contributions and interest in full satisfaction of all rights and benefits under this Retirement System except that a member terminating with at least five (5) years of service may elect to leave the accumulated contributions and interest on deposit with option of reciprocity.

DEFERRED RETIREMENT

Contributions left on deposit by a member terminating with at least five (5) years of service (vesting) entitle the employee to a retirement annuity upon attaining age 55.

RECIPROCITY

Effective December 9, 1994, the City entered into an agreement with the California Public Employees' Retirement System (PERS) that extends reciprocal benefits to members. In certain situations, this agreement results in improved retirement benefits for members who move from one eligible retirement system to another. If a member terminates and goes to a California PERS agency or a reciprocal agency and claims reciprocity, they may leave their accumulated contributions and interest on deposit regardless of years of service.

COST OF LIVING

Effective April 1, 2006, the cost-of-living (COL) provision provides a flat 3% annual adjustment in April for retirees and survivors.

DEATH BEFORE RETIREMENT

The surviving spouse of an eligible employee who dies before retirement will receive a retirement allowance determined by the years of service times 2.5% times the final average salary (minimum of 40% and maximum of 75%). Unmarried children are entitled to an allowance to age 18 (22 if they are full time students) if there is no spouse. The allowance is as follows:

1 child receives 25% of the spousal benefit
2 children share 50% of the spousal benefit
3+ children share 75% of the spousal benefit

The beneficiary, in the event that no family members are eligible for a monthly allowance, is entitled to a return of the member's contributions and interest plus a death benefit of one month's salary for each year of service (up to six years).

If the employee is 55 and has 20 or more years of service at the time of death, his/her spouse will retain the survivorship allowance for life. If not, the spouse loses the allowance upon a remarriage.

Summary of the Principal System Provisions *Continued*

DEATH AFTER RETIREMENT

The surviving spouse receives one-half* of the member's retirement allowance until death and a $500 death benefit (*At the time of retirement, the member may select an alternative option allowing for a survivorship allowance of up to 100% of the member's allowance). If there is no surviving spouse, dependent children are eligible for an allowance. The allowance is:

1 child receives 25% of spousal benefit
2 children share 50% of spousal benefit
3+ children share 75% of spousal benefit

MANAGEMENT

The System is under the management of a seven (7) member Board of Administration consisting of two City Council members, a Civil Service Commissioner, a public member with significant banking or investment experience, a retiree representative, and two elected employees who are members of the Retirement System.

ADMINISTRATION

A full-time Director is employed by the City. He serves as Secretary and Chief Executive Officer to the Board of Administration.

The Fund pays the cost of the personnel who are employed for the purpose of managing the Retirement System. It also pays any directly related administrative costs.

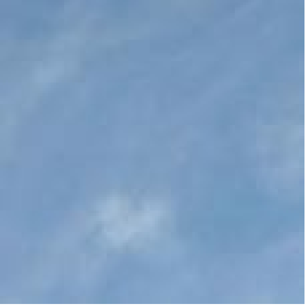
The Northern Trust is employed as custodian of fund assets and collector of investment income.

ACTUARIAL SOUNDNESS

Gabriel, Roeder, Smith & Company is retained for regular, continuing actuarial services. Plan and benefit provisions are periodically reviewed to assure continuing soundness.

INVESTMENT AUTHORITY AND POLICY

The investment authority is broad and allows maximum utilization of the System's resources. Nationally known investment advisory services including American Realty Advisors; Atlanta Capital Management; BlackRock Financial Management; Boston Company Asset Management; Brandywine Asset Management; Dodge and Cox; DRA Advisors; Eagle Asset Management; Fidelity Investments; Fisher Investments Institutional Group; Loomis Sayles; McKinley Capital Management; MIG Realty Advisors; Northern Trust; Pantheon Ventures, Inc.; Pathway Capital Management, LLC; Prudential Real Estate Investors; and Wellington Management are retained for full-time investment counsel. The Northern Trust is retained as the investment performance consultant and Strategic Investment Solutions, Inc. as the investment consultant.



San José Federated City Employees' Retirement System

Comprehensive Annual Financial Report 2006 – 2007

Financial Section

Independent Auditor's Report

MACIAS GINI & O'CONNELL LLP
CERTIFIED PUBLIC ACCOUNTANTS & MANAGEMENT CONSULTANTS

300 S Street, Suite 300
Sacramento, CA 95816
916-928-4600 phone

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Walnut Creek, CA 94596
925-274-0190

505 14th Street, 5th Floor
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510-273-8974

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213-286-6400

402 West Broadway, Suite 400
San Diego, CA 92101
619-573-1112

Board of Administration
City of San José
Federated City Employees' Retirement System
1737 North First Street, Suite 580
San José, CA 95112-4505

INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying statements of plan net assets of the City of San José Federated City Employees' Retirement System (System), a pension trust fund of the City of San José, California, as of June 30, 2007 and 2006, and the related statements of changes in plan net assets for the fiscal years then ended. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 2(a), the financial statements of the System are intended to present only the plan net assets and changes in plan net assets of the System. They do not purport to, and do not, present fairly the financial position of the City of San José, California, as of June 30, 2007 and 2006, and the changes in its financial position for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the System as of June 30, 2007 and 2006, and the results of its operations for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Independent Auditor's Report *Continued*

MACIAS GINI & O'CONNELL LLP
CERTIFIED PUBLIC ACCOUNTANTS & MANAGEMENT CONSULTANTS

In accordance with Government Auditing Standards, we have also issued our report dated October 26, 2007 on our consideration of the System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

The management's discussion and analysis and the schedules designated as other required supplementary information in the table of contents are not a required part 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 audit was conducted for the purpose of forming an opinion on the System's basic financial statements. The introductory section, other supplementary information in the financial section, the investment, actuarial and statistical sections listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. The other supplementary information in the financial section has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory, investment, actuarial and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

Macias Gini & O'Connell LLP

Certified Public Accountants
Walnut Creek, California
October 26, 2007

Management's Discussion and Analysis (Unaudited)

City of San José
Department of Retirement Services
Board of Administration
Federated City Employees' Retirement System
1737 North First Street, Suite 580
City of San José
San José, California 95112-4505

Edward F. Overton
Director, Retirement Services

We are pleased to provide this overview and analysis of the financial activities of the Federated City Employees' Retirement System (the System) for the fiscal years ended June 30, 2007 and 2006. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our Letter of Transmittal, which begins on page 2 of this report.

Financial Highlights for Fiscal Year 2007

- The net assets of the System at the close of the fiscal year 2007 are $1,862,998,000 (net assets held in trust for pension benefits and postemployment healthcare benefits). All of the net assets are available to meet the System's ongoing obligations to plan participants and their beneficiaries except the Supplemental Retiree Benefit Reserve of $18,590,000.
- The System's total net assets held in trust for pension benefits and postemployment healthcare benefits increased by $239,042,000 or 14.7%, primarily as a result of a strengthening in the investment market.
- Additions to Plan Net Assets for the year were $341,267,000, which includes member and employer contributions of $83,714,000, net investment income of $257,047,000, and net securities lending income of $506,000.
- Deductions in Plan Net Assets increased from $93,202,000 to $102,225,000 over the prior year, or approximately 9.7% due to an increase in retirement and healthcare benefits, which was attributable to enhanced benefits and an increased number of beneficiaries along with increased health premium costs.

Overview of the Financial Statements

The following discussion and analysis is intended to serve as an introduction to the System's financial statements, which are comprised of these components:

1. Statement of Plan Net Assets
2. Statement of Changes in Plan Net Assets
3. Notes to the Basic Financial Statements

Please note, however, that this report also contains other supplementary information in addition to the basic financial statements themselves.

The ***Statement of Plan Net Assets*** is a snapshot of account balances at fiscal year-end. It indicates the assets available for future payments to retirees and any current liabilities that are owed at this time.

The ***Statement of Changes in Plan Net Assets,*** on the other hand, provides a view of current year additions to and deductions from the System.

Both statements are in compliance with generally accepted accounting principles (GAAP) as set forth by the Governmental Accounting Standards Board. GAAP requires certain disclosures and state and local government pension plan reports use the full accrual method of accounting. The System complies with all material requirements of these pronouncements.

The ***Statement of Plan Net Assets*** and the ***Statement of Changes in Plan Net Assets*** report information about the System's activities. These statements include all assets and liabilities, using the full accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's additions and deductions are taken into account regardless of when cash is received or paid. All investment gains and losses are shown at trade date, not settlement date. In addition, both realized and unrealized gains and losses are shown on investments.

These two statements report the System's net assets held in trust for pension benefits and postemployment healthcare benefits (net assets)—the difference between assets and liabilities. Over time, increases and decreases in the System's net assets are one indicator of whether its financial health is improving or deteriorating. Other factors, such as market conditions, should also be considered in measuring the System's overall health (see the System's financial statements beginning on page 20 of this report).

Notes to the Basic Financial Statements provide additional information that is essential to a full understanding of the data provided in the financial statements (see Notes to Basic Financial Statements on page 24 of this report).

Management's Discussion and Analysis (Unaudited) *Continued*

Other Information. In addition to the financial statements and accompanying notes, this report presents certain required supplementary information concerning the System's progress in funding its obligations to provide pension benefits to members, employer contributions and actuarial methods and assumptions (see Other Required Supplementary Information beginning on page 37 of this report).

The combining schedules, schedules of administrative expenses, investment manager fees and other investment expenses, and payments to consultants are presented immediately following the required supplementary information on pensions.

Financial Analysis

As previously noted, net assets may serve over time as a useful indication of the System's financial position (see Tables 1a on page 14). The assets of the System exceeded its liabilities at the close of fiscal year 2007 and 2006.

As of June 30, 2007, $1,862,998,000 in total net assets was held in trust for pension benefits and postemployment healthcare benefits (see Table 1a on page 14). All of the net assets are available to meet the System's ongoing obligation to plan participants and their beneficiaries, except assets held in the Supplemental Retiree Benefit Reserve of $18,590,000, which is used to provide supplemental benefits to retirees on a discretionary basis.

As of June 30, 2006, $1,623,956,000 in total net assets was held in trust for pension benefits and postemployment healthcare benefits (see Table 1b on page 14). This total represented an increase of 7.4% in net assets over the prior year primarily due to an increase in the fair value of investments.

As of June 30, 2007, total net assets increased by 14.7% over the prior year primarily due to an increase in investments at fair value, which increased $219,055,000 from the prior year.

As of June 30, 2006, total net assets increased by 7.4% over the prior year primarily due to appreciation in the fair value of investments which increased $109,237,000.

As of June 30, 2007, receivables increased by $72,822,000, or 233.8% mainly due to an increase in receivables from brokers and others. In the previous year, receivables decreased by $20,781,000, or 40.0% due to a decrease in receivables from brokers and other.

As of June 30, 2007, total liabilities increased by $161,967,000, or 81.9%, compared with June 30, 2006, mainly due to an increase in payables to brokers and securities lending collateral due to borrowers.

As of June 30, 2006, total liabilities decreased by $40,516,000, or 17.0%, compared with June 30, 2005, also due mainly to a decrease in payables to brokers and securities lending collateral due to borrowers.

Reserves

The System's reserves are established from contributions and the accumulation of investment income, after satisfying investment and administrative expenses (see table on page 26). The Defined Benefit Pension Plan Net Assets are allocated between the Retirement Fund, which includes postemployment healthcare benefits, and the Cost-of-Living Fund.

The appreciation in the fair value of investments and the five-year smoothing of investment gains and losses resulted in an increase in the "unrealized gains (loss) on investments held" reserve of $156,437,000 and $59,189,000 as of June 30, 2007 and 2006, respectively. These amounts are components of the general reserve.

Management's Discussion and Analysis (Unaudited) *Continued*

FCERS NET ASSETS (Table 1a)

As of June 30, 2007 and 2006

	2007	*2006*	*Increase Amount*	*Increase Percent*
Receivables	$ 103,973,000	$ 31,151,000	$ 72,822,000	233.8%
Investments at Fair Value	2,118,675,000	1,790,488,000	328,187,000	18.3%
Total Assets	**2,222,648,000**	**1,821,639,000**	**401,009,000**	**22.0%**
Current Liabilities	359,650,000	197,683,000	161,967,000	81.9%
Total Liabilities	**359,650,000**	**197,683,000**	**161,967,000**	**81.9%**
NET ASSETS	**$1,862,998,000**	**$1,623,956,000**	**$239,042,000**	**14.7%**

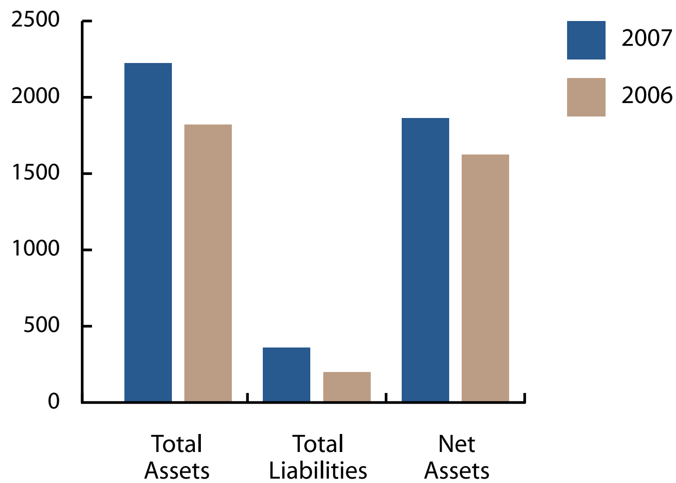
FCERS NET ASSETS (Table 1b)

As of June 30, 2006 and 2005

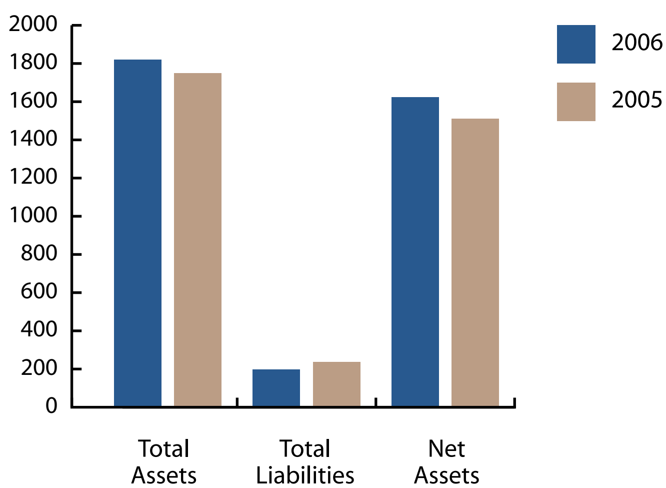
	2006	*2005*	*Increase/(Decrease) Amount*	*Increase/(Decrease) Percent*
Receivables	$ 31,151,000	$ 51,932,000	$ (20,781,000)	(40.0%)
Investments at Fair Value	1,790,488,000	1,698,430,000	92,058,000	5.4%
Total Assets	**1,821,639,000**	**1,750,362,000**	**71,277,000**	**4.1%**
Current Liabilities	197,683,000	238,199,000	(40,516,000)	(17.0%)
Total Liabilities	**197,683,000**	**238,199,000**	**(40,516,000)**	**(17.0%)**
NET ASSETS	**$1,623,956,000**	**$1,512,163,000**	**$111,793,000**	**7.4%**

Management's Discussion and Analysis (Unaudited) *Continued*

FCERS NET ASSETS
As of June 30, 2007 and 2006
(Dollars in Millions)



FCERS NET ASSETS
As of June 30, 2006 and 2005
(Dollars in Millions)



Management's Discussion and Analysis (Unaudited) *Continued*

ADDITIONS TO PLAN NET ASSETS (Table 2a)

For the Fiscal Years Ended June 30, 2007 and 2006

	2007	*2006*	*Increase Amount*	*Increase Percent*
Employee Contributions	$ 21,982,000	$ 17,621,000	$ 4,361,000	24.7%
Employer Contributions	61,732,000	47,228,000	14,504,000	30.7%
Net Investment Income*	257,047,000	139,764,000	117,283,000	83.9%
Net Securities Lending Income	506,000	382,000	124,000	32.5%
TOTAL ADDITIONS	**$341,267,000**	**$204,995,000**	**$136,272,000**	**66.5%**

**Net of Investment Expenses of $6,842,000 and $5,231,000 in 2007 and 2006, respectively*

ADDITIONS TO PLAN NET ASSETS (Table 2b)

For the Fiscal Years Ended June 30, 2006 and 2005

	2006	*2005*	*Increase/(Decrease) Amount*	*Increase/(Decrease) Percent*
Employee Contributions	$ 17,621,000	$ 17,612,000	$ 9,000	0.1%
Employer Contributions	47,228,000	47,548,000	(320,000)	(0.7%)
Net Investment Income*	139,764,000	121,943,000	17,821,000	14.6%
Net Securities Lending Income	382,000	214,000	168,000	78.5%
TOTAL ADDITIONS	**$204,995,000**	**$187,317,000**	**$ 17,678,000**	**9.4%**

**Net of Investment Expenses of $5,231,000 and $4,538,000 in 2006 and 2005, respectively*

DEDUCTIONS TO PLAN NET ASSETS (Table 3a)

For the Fiscal Years Ended June 30, 2007 and 2006

	2007	*2006*	*Increase/(Decrease) Amount*	*Increase/(Decrease) Percent*
Retirement Benefits	$ 75,135,000	$ 68,438,000	$ 6,697,000	9.8%
Healthcare Insurance Premiums	18,265,000	15,904,000	2,361,000	14.8%
Death Benefits	5,867,000	5,721,000	146,000	2.6%
Refund of Contributions	1,008,000	1,246,000	(238,000)	(19.1%)
Administrative and other	1,950,000	1,893,000	57,000	3.0%
TOTAL DEDUCTIONS	**$102,225,000**	**$ 93,202,000**	**$ 9,023,000**	**9.7%**

DEDUCTIONS TO PLAN NET ASSETS (Table 3b)

For the Fiscal Years Ended June 30, 2006 and 2005

	2006	*2005*	*Increase Amount*	*Increase Percent*
Retirement Benefits	$ 68,438,000	$ 60,438,000	$ 8,000,000	13.2%
Healthcare Insurance Premiums	15,904,000	13,393,000	2,511,000	18.7%
Death Benefits	5,721,000	5,437,000	284,000	5.2%
Refund of Contributions	1,246,000	927,000	319,000	34.4%
Administrative and other	1,893,000	1,683,000	210,000	12.5%
TOTAL DEDUCTIONS	**$ 93,202,000**	**$ 81,878,000**	**$11,324,000**	**13.8%**

Management's Discussion and Analysis (Unaudited) *Continued*

CHANGES IN PLAN NET ASSETS (Table 4a)

For the Fiscal Years Ended June 30, 2007 and 2006

	2007	*2006*	*Increase Amount*	*Increase Percent*
Total Additions	$ 341,267,000	$ 204,995,000	$ 136,272,000	66.5%
Total Deductions	102,225,000	93,202,000	9,023,000	9.7%
NET INCREASE IN PLAN ASSETS	**$239,042,000**	**$111,793,000**	**$127,249,000**	**113.8%**

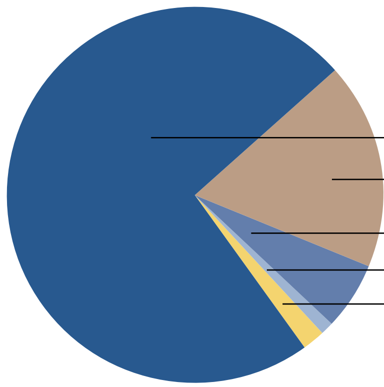
CHANGES IN PLAN NET ASSETS (Table 4b)

For the Fiscal Years Ended June 30, 2006 and 2005

	2006	*2005*	*Increase Amount*	*Increase Percent*
Total Additions	$ 204,995,000	$ 187,317,000	$ 17,678,000	9.4%
Total Deductions	93,202,000	81,878,000	11,324,000	13.8%
NET INCREASE IN PLAN ASSETS	**$111,793,000**	**$105,439,000**	**$ 6,354,000**	**6.0%**

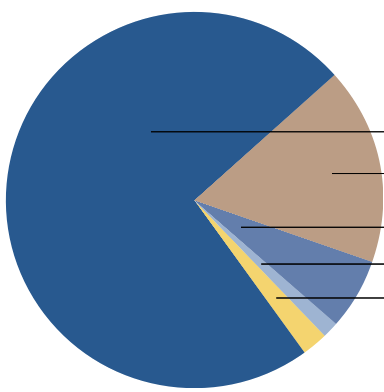
Management's Discussion and Analysis (Unaudited) *Continued*

DEDUCTIONS TO PLAN NET ASSETS 2007



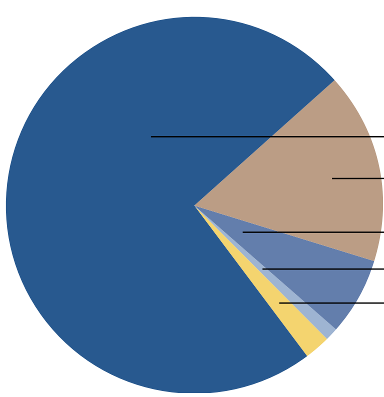
Retirement Benefits	73.5%	$75,135,000
Healthcare Insurance Premiums	17.9%	$18,265,000
Death Benefits	5.7%	$5,867,000
Refund of Contributions	1.0%	$1,008,000
Administrative and Other	1.9%	$1,950,000

DEDUCTIONS TO PLAN NET ASSETS 2006



Retirement Benefits	73.4%	$68,438,000
Healthcare Insurance Premiums	17.1%	$15,904,000
Death Benefits	6.2%	$5,721,000
Refund of Contributions	1.3%	$1,246,000
Administrative and Other	2.0%	$1,893,000

DEDUCTIONS TO PLAN NET ASSETS 2005



Retirement Benefits	73.8%	$60,438,000
Healthcare Insurance Premiums	16.4%	$13,393,000
Death Benefits	6.6%	$5,437,000
Refund of Contributions	1.1%	$927,000
Administrative and Other	2.1%	$1,683,000

Management's Discussion and Analysis (Unaudited) *Continued*

FCERS ACTIVITIES

The market appreciation during fiscal year 2007 resulted in increased net assets by $239,042,000, thereby accounting for a 14.7% increase over the prior year. Key elements of this increase are described in the sections that follow.

Additions to Plan Net Assets

The assets needed to finance retirement benefits are accumulated through the collection of employer and employee contributions and through earnings on investments (net of investment expense). Additions for the fiscal year ended June 30, 2007, totaled $341,267,000 (see Table 2a on page 16).

By the fiscal year ended June 30, 2007, overall additions had increased by $136,272,000, or 66.5% from the prior year primarily due to an increase in net investment income, which increased by $117,283,000 or 83.9%. The System's time-weighted rate of return for the fiscal year ended June 30, 2007 was 16.22% versus 10.81% for the fiscal year 2005-06.

Additions for the fiscal year ended June 30, 2006 totaled $204,995,000, representing an increase of $17,678,000 or 9.4%, from the prior year also primarily due to an increase in net investment income which increased $17,821,000, or 14.6% (see Table 2b on page 16). The increase in net investment income was due to an increase in net appreciation in fair value of investments.

Deductions from Plan Net Assets

The System was created to provide lifetime retirement annuities, survivor benefits and permanent disability benefits to qualified members and their beneficiaries. The cost of such programs includes recurring benefit payments, as designated by the System, refund of contributions to terminated employees, and the cost of administering the System.

Deductions for the fiscal year ended June 30, 2007 totaled $102,225,000, an increase of 9.7% over fiscal year ended June 30, 2006 (see Table 3a on page 16). Increases in retirement benefits of $6,697,000, and healthcare insurance premiums of $2,361,000, were the primary reasons for the increase in deductions. Retirement benefits increased due to benefit enhancements and increased number of beneficiaries. Healthcare insurance costs increased due to higher premiums and administrative expenses which increased primarily as a result of an increase in payroll costs due to increased staffing.

Deductions for the fiscal year ended June 30, 2006 totaled $93,202,000, an increase of 13.8% over fiscal year ended June 30, 2005 (see Table 3b on page 16). Increases in retirement benefits of $8,000,000, and healthcare insurance premiums of $2,511,000, were the primary reasons for the increase in deductions. Retirement benefits increased due to benefit enhancements and increased number of beneficiaries. Healthcare insurance costs increased due to higher premiums and administrative expenses.

The System's Fiduciary Responsibilities

The System's Board and management staff are fiduciaries of the pension trust fund. Under the California Constitution the assets can only be used for the exclusive benefit of plan participants and their beneficiaries.

Economic Factors and Rates Affecting Next Year

The System will conduct a new actuarial valuation using the June 30, 2007 data. It is anticipated that the funding ratio will improve from that of June 30, 2005, which was approximately 81.0% due to the fact that all of the prior year's negative return has been recognized.

In fiscal year 2007, the System completed an actuarial valuation for the post employment health benefits. The study resulted in the recognition of an unfunded actuarial accrued liability of $621,650,665. The System is required to disclose this liability in the System's notes to basic financial statements. The City is currently working on a plan to mitigate the impact of this liability.

Requests for Information

This financial report is designed to provide the Board of Administration, Mayor and City Council, our membership, taxpayers, and investment managers with a general overview of the System's finances and to account for the money it receives. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to:

Federated City Employees' Retirement System
1737 North First Street, Suite 580
San José, California 95112-4505

Respectfully Submitted,

Edward F. Overton
Director, Retirement Services

Basic Financial Statements

STATEMENTS OF PLAN NET ASSETS

June 30, 2007 and 2006

(Dollars in thousands)	*2007* Pension Benefits	Postemployment Healthcare Benefits	Total
ASSETS			
Employee contributions	$ 466	$ 364	$ 830
Employer contributions	2,034	428	2,462
Brokers and others	89,030	4,908	93,938
Accrued investment income	6,389	354	6,743
Total receivables	**97,919**	**6,054**	**103,973**
Investments, at fair value:			
Securities and other:			
U.S. Treasury notes and bonds	38,685	2,102	40,787
U.S. government agency securities	238,594	12,966	251,560
International government bonds	59,694	3,244	62,938
Domestic corporate bonds	199,432	10,838	210,270
International corporate bonds	36,880	2,004	38,884
Domestic equity securities	744,129	40,438	784,567
International equity securities	329,829	17,924	347,753
Private market equity	25,567	1,389	26,956
International forward currency contracts	(39)	(2)	(41)
Collective short-term investment funds	75,641	4,110	79,751
Real estate	77,140	4,192	81,332
Securities lending cash collateral investment pool	183,786	10,132	193,918
Total investments	**2,009,338**	**109,337**	**2,118,675**
TOTAL ASSETS	**2,107,257**	**115,391**	**2,222,648**
LIABILITIES			
Payable to brokers	155,529	8,574	164,103
Securities lending collateral due to borrowers	183,786	10,132	193,918
Other liabilities	1,545	84	1,629
TOTAL LIABILITIES	**340,860**	**18,790**	**359,650**
NET ASSETS HELD IN TRUST FOR			
Pension benefits	1,766,397	-	1,766,397
Postemployment healthcare benefits	-	96,601	96,601
TOTAL NET ASSETS*	**$1,766,397**	**$ 96,601**	**$1,862,998**

**A schedule of funding progress is presented on page 37.*
See accompanying notes to basic financial statements.

Continued

Basic Financial Statements *Continued*

STATEMENTS OF PLAN NET ASSETS *Continued*

June 30, 2007 and 2006

(Dollars in thousands)	2006 *Pension Benefits*	2006 *Postemployment Healthcare Benefits*	2006 *Total*
ASSETS			
Receivables:			
Employee contributions	$ 441	$ 187	$ 628
Employer contributions	1,617	233	1,850
Brokers and others	21,212	1,133	22,345
Accrued investment income	6,006	322	6,328
Total receivables	**29,276**	**1,875**	**31,151**
Investments, at fair value:			
Securities and other:			
U.S. Treasury notes and bonds	65,702	3,449	69,151
U.S. government agency securities	170,592	8,956	179,548
International government bonds	61,368	3,222	64,590
Domestic corporate bonds	190,697	10,011	200,708
International corporate bonds	34,973	1,836	36,809
Domestic equity securities	670,930	35,222	706,152
International equity securities	277,486	14,567	292,053
Private market equity	7,559	397	7,956
International forward currency contracts	56	3	59
Collective short-term investment funds	29,303	1,538	30,841
Real estate	51,862	2,722	54,584
Securities lending cash collateral investment pool	140,532	7,505	148,037
Total investments	**1,701,060**	**89,428**	**1,790,488**
TOTAL ASSETS	**1,730,336**	**91,303**	**1,821,639**
LIABILITIES			
Payable to brokers	45,171	2,412	47,583
Securities lending collateral due to borrowers	140,532	7,505	148,037
Other liabilities	1,965	98	2,063
TOTAL LIABILITIES	**187,668**	**10,015**	**197,683**
NET ASSETS HELD IN TRUST FOR			
Pension benefits	1,542,668	-	1,542,668
Postemployment healthcare benefits	-	81,288	81,288
TOTAL NET ASSETS*	**$1,542,668**	**$81,288**	**$1,623,956**

**A schedule of funding progress is presented on page 37.*
See accompanying notes to basic financial statements.

Basic Financial Statements *Continued*

STATEMENTS OF CHANGES IN PLAN NET ASSETS

For the Fiscal Years Ended June 30, 2007 and 2006

(Dollars in thousands)	*2007* Pension Benefits	Postemployment Healthcare Benefits	Total
ADDITIONS			
Contributions:			
Employee	$ 12,370	$ 9,612	$ 21,982
Employer	51,004	10,728	61,732
Total Contributions	**63,374**	**20,340**	**83,714**
Investment income:			
Net appreciation in fair value of investments	207,706	11,349	219,055
Interest income	30,204	1,649	31,853
Dividend income	8,429	460	8,889
Net rental income	3,880	212	4,092
Less investment expense	(6,489)	(353)	(6,842)
Net investment income before securities lending income	**243,730**	**13,317**	**257,047**
Securities lending income:			
Earnings	9,634	526	10,160
Rebates	(8,994)	(491)	(9,485)
Fees	(160)	(9)	(169)
Net securities lending income	**480**	**26**	**506**
Net investment income	**244,210**	**13,343**	**257,553**
TOTAL ADDITIONS	**307,584**	**33,683**	**341,267**
DEDUCTIONS			
Retirement benefits	75,135	-	75,135
Healthcare insurance premiums	-	18,265	18,265
Death benefits	5,867	-	5,867
Refund of contributions	1,008	-	1,008
Administrative expenses and other	1,845	105	1,950
TOTAL DEDUCTIONS	**83,855**	**18,370**	**102,225**
NET INCREASE	**223,729**	**15,313**	**239,042**
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS & POST-EMPLOYMENT HEALTHCARE BENEFITS			
Beginning of Year	**1,542,668**	**81,288**	**1,623,956**
End of Year	**$1,766,397**	**$96,601**	**$1,862,998**

Continued

See accompanying notes to basic financial statements.

Basic Financial Statements *Continued*

STATEMENTS OF CHANGES IN PLAN NET ASSETS *Continued*

For the Fiscal Years Ended June 30, 2007 and 2006

(Dollars in thousands)	*2006* Pension Benefits	Postemployment Healthcare Benefits	Total
ADDITIONS			
Contributions:			
Employee	$ 12,395	$ 5,226	$ 17,621
Employer	41,267	5,961	47,228
Total Contributions	**53,662**	**11,187**	**64,849**
Investment income:			
Net appreciation in fair value of investments	103,564	5,673	109,237
Interest income	25,526	1,397	26,923
Dividend income	7,470	409	7,879
Net rental income	907	49	956
Less investment expense	(4,957)	(274)	(5,231)
Net investment income before securities lending income	**132,510**	**7,254**	**139,764**
Securities lending income:			
Earnings	6,603	361	6,964
Rebates	(6,074)	(333)	(6,407)
Fees	(166)	(9)	(175)
Net securities lending income	**363**	**19**	**382**
Net investment income	**132,873**	**7,273**	**140,146**
TOTAL ADDITIONS	**186,535**	**18,460**	**204,995**
DEDUCTIONS			
Retirement benefits	68,438	-	68,438
Healthcare insurance premiums	-	15,904	15,904
Death benefits	5,721	-	5,721
Refund of contributions	1,246	-	1,246
Administrative expenses and other	1,790	103	1,893
TOTAL DEDUCTIONS	**77,195**	**16,007**	**93,202**
NET INCREASE	**109,340**	**2,453**	**111,793**
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS & POST-EMPLOYMENT HEALTHCARE BENEFITS			
Beginning of Year	**1,433,328**	**78,835**	**1,512,163**
End of Year	**$1,542,668**	**$81,288**	**$1,623,956**

See accompanying notes to basic financial statements.

Notes to Basic Financial Statements

For The Fiscal Years Ended June 30, 2007 and 2006

NOTE 1 – DESCRIPTION OF THE PLAN

The following description of the City of San José Federated City Employees' Retirement System (System) is provided for general information purposes only. Employees and members should refer to the City of San José Municipal Code for more complete information.

(a) General

The System, consisting of a single employer Defined Benefit Pension Plan and a Postemployment Healthcare Plan, was established in 1941 and last amended June 16, 2006, to provide retirement benefits for certain employees of the City of San José (City). The System is considered to be a part of the City's financial reporting entity and is included in the City's basic financial statements as a pension trust fund. The System is administered by the Director of Retirement, an employee of the City, under the direction of the Federated City Employees' Retirement System Board of Administration (Board of Administration). The contribution and benefit provisions and all other requirements are established by City ordinance. The System is responsible for all direct administrative costs, which are funded by investment earnings, except for certain support services, which are provided by the City.

All full-time and eligible part-time employees of the City, except employees who are members of the City's Police and Fire Department Retirement Plan, are required to be members of the System. Total payroll, except for Police and Fire employees, amounted to approximately $305,088,000 and $290,581,000 for 2007 and 2006, respectively. Covered payroll amounted to approximately $280,575,000 and $274,592,000 for 2007 and 2006, respectively.

Participants of the Postemployment Healthcare Plan are also participants of the Defined Benefit Pension Plan. As of June 30, 2007 and 2006, employee membership data related to the System was as follows:

Defined Benefit Pension Plan	2007	2006
Retirees and beneficiaries currently receiving benefits	2,749	2,621
Terminated vested members not yet receiving benefits	530	458
Active members	4,143	4,066
TOTAL	**7,422**	**7,145**

Postemployment Healthcare Plan	2007	2006
Retirees and beneficiaries currently receiving benefits	2,053	1,963
Terminated vested members not yet receiving benefits	77	62
Active members	4,143	4,066
TOTAL	**6,273**	**6,091**

The System is not subject to the provisions of the Employee Retirement Income Security Act of 1974.

(b) Pension Benefits

An employee with five or more years of service who reaches the normal retirement age of 55, or an employee of any age with 30 years of service, is entitled to annual pension benefits equal to 2.5% of final average annual salary for each year of service up to a maximum benefit of 75% of final compensation. Final compensation is the average annual salary during the highest 12 months of consecutive service. In addition, retirement benefits are adjusted for an annual cost-of-living allowance (COLA). The current maximum increase in the COLA is 3% per year.

If employees terminate employment and elect to receive a return of contributions, the accumulated plan benefits attributable to the City's contributions is forfeited; however, an employee's accumulated contribution plus earnings thereon is refunded. Refunds are paid out on a lump-sum basis. The forfeited amount of the City's contributions remains in the System. In the case of reciprocity, the member may leave contributions in the System with less than five years of service.

Effective December 9, 1994, the System entered into an agreement with the California Public Employees' Retirement System (PERS) that extends reciprocal retirement benefits to members. In certain situations, this agreement results in improved retirement benefits for members who move from one eligible retirement system to another.

(c) Death Benefits

If an employee's death before retirement is service related, or is non-service related (employee has at least five years of service), a surviving spouse or domestic partner is paid an annual annuity benefit equal to 2.5% of final compensation multiplied by the number of years of service (minimum of 40% and maximum of 75% of final compensation) until he or she remarries or dies. Deferred vested members are not eligible for the 40% minimum. The allowance will continue even if the spouse or domestic partner remarries if the member was at least 55 years old and had at least 20 years of service. If there is no surviving

Notes to Basic Financial Statements *Continued*

NOTE 1 – DESCRIPTION OF THE PLAN *Continued*

spouse or domestic partner, unmarried children up to 18 years of age, or up to 22 years of age if a full-time student, are entitled to a benefit payment based on the spousal or domestic partner benefit such that no one child shall receive more than 25% of the spousal or domestic partner benefit and the sum for all eligible children shall not exceed 75% of the spousal or domestic partner benefit. If no family members are eligible, the employee's contributions plus one month's salary for each year of service up to a maximum of six years of service are returned to the employee's beneficiary or estate.

If an employee dies after retirement, $500 is paid to the employee's beneficiary or estate. In addition, the employee's surviving spouse or domestic partner continues to receive, for life, 50% of the employee's annual pension benefit as defined above. If there is no surviving spouse or domestic partner, 25% of the spouse or domestic partner's benefit payment is made to each eligible child as defined above, but the maximum benefit to children cannot exceed 75% of the benefit that would have been paid to a surviving spouse or domestic partner.

(d) Disability Benefits

If an employee suffers a service related disability before retirement, the annual disability benefit paid is 40% of final average salary. The maximum benefit is 75% of final average salary. For members with more than 16 years of service, the monthly retirement allowance is the final average salary multiplied by 40% plus the final average salary multiplied by 2.5% for each year over 16.

If an employee with at least five years of service suffers a non-service related disability, the annual disability benefit is equal to the greater of: (1) 2.5% of final compensation multiplied by the number of years of service, up to a maximum of 30 years; or (2) 40% of final compensation. The benefit is reduced by 0.5% of final compensation for each year an employee's age is under 55.

If an employee was hired on or after September 1, 1998, the benefit is calculated using the following formula: 20% of final compensation, plus 2% for each year of service in excess of six but less than 16, plus 2.5% for years of service in excess of 16.

(e) Postemployment Healthcare Benefits

The City of San José Municipal Code provides that retired employees with 15 or more years of service, their survivors, or those retired employees who are receiving at least 37.5% of final compensation are entitled to payment of 100% of the lowest priced medical insurance plan available to an active Federated City employee. Members and eligible survivors must pay for the difference between the amount of the premium for their selected plan and the portion paid by the System. However, the System pays the entire premium cost for dental insurance coverage.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of Presentation

The System is reported in a pension trust fund in the City of San José's basic financial statements. The financial statements of the System present only the financial activities of the System and are not intended to present the financial position and changes in financial position of the City of San José in conformity with accounting principles generally accepted in the United States of America (GAAP).

(b) Basis of Accounting

The financial statements of the System are prepared on the accrual basis of accounting. Contributions are recognized as revenue when due pursuant to formal commitments as well as statutory and contractual commitments (at the end of the pay period). Benefits and refunds of contributions are recognized when due and payable under the provisions of the Plan. Activities of the Defined Benefit Pension Plan and the Post-employment Healthcare Plan are accounted for separately. It is required by the municipal code that transactions of the Defined Benefit Pension Plan be accounted for in two funds: a Retirement Fund and a Cost-of-Living Fund.

The preparation of the financial statements in conformity with GAAP requires management to make certain estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from those estimates.

(c) Investments

Investments are reported at fair value. Securities traded on a national or international exchange are valued at the last reported sales price on the last business day of the fiscal year at current exchange rates, if applicable. Investments that do not have an established market are reported at estimated fair value. The fair value of the private equities are based on actual cash flows to/from the System and the transactions and unrealized gain/loss as ascertained from the most recently available investor reports or financial statements issued by the manager of those funds. The fund manager provides an estimated unrealized gain/loss of the fund based on the financial statements and other portfolio information received from their underlying portfolio partnerships. The System's investments in pooled funds have the underlying securities valued by the fund manager in accordance with the above standards. As of June 30, 2007, the

NOTES TO BASIC FINANCIAL STATEMENTS *Continued*

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *Continued*

System had the following pooled fund holdings: $412,624,000 in domestic equities, $106,014,000 in international equities, and $26,956,000 in private equities. As of June 30, 2006 the amounts were $362,225,000 in domestic equities, $99,311,000 in international equities, and $7,956,000 in private equities.

Purchases and sales of securities are reflected on the trade date. Investment income is recognized as earned. Rental income is recognized as earned, net of expenses.

(d) Plan Net Assets Held in Trust for Pension and Postemployment Healthcare Benefits

The System is required by the City of San José Municipal Code to establish various reserves in the plan net assets. The Plan Net Assets are allocated between the Defined Benefit Pension Plan (which includes the Retirement Fund and the Cost-of-Living Fund) and the Postemployment Healthcare Plan. As of June 30, 2007 and 2006, the net assets, totaling $1,862,998,000 and $1,623,956,000, respectively, are allocated as follows:

Employee Contributions Reserve is a fully funded reserve that represents the total accumulated employee contributions of current active and deferred members plus credited interest. The reserve is accounted for separately due to the possibility of their return to the member upon separation from City employment.

Supplemental Retiree Benefit Reserve is a fully funded reserve that represents 10% of total accumulated excess earnings plus credited interest.

General Reserve is a fully funded reserve that represents net earnings resulting from interest earnings, realized and unrealized investment gains and losses. The unrealized gains and losses for fiscal year 2007 and 2006 were $356,282,000 and $199,845,000, respectively. General Reserve also represents an accumulation of funds necessary to pay all accumulated vested retirement obligations.

(Dollars in thousands)	*Retirement Fund*	*Cost-of-Living Fund*	*Total Defined Benefit Pension Benefits Plan*	*Postemployment Healthcare Plan*	*Total*
June 30, 2007:					
Employee contributions	$ 173,744	$ 46,981	$ 220,725	$ 12,857	$ 233,582
Supplemental retiree benefit	18,590	-	18,590	-	18,590
General reserve	1,113,002	414,080	1,527,082	83,744	1,610,826
TOTAL	**$1,305,336**	**$461,061**	**$1,766,397**	**$96,601**	**$1,862,998**
June 30, 2006:					
Employee contributions	$ 166,028	$ 46,944	$ 212,972	$ 11,844	$ 224,816
Supplemental retiree benefit	16,488	-	16,488	-	16,488
General reserve	956,970	356,238	1,313,208	69,444	1,382,652
TOTAL	**$1,139,486**	**$403,182**	**$1,542,668**	**$81,288**	**$1,623,956**

Notes to Basic Financial Statements *Continued*

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *Continued*

(e) Reclassifications

Certain amounts in fiscal year 2006 have been reclassified to conform with the fiscal year 2007 presentation.

(f) Implementation of Governmental Accounting Standards Board Statements

For fiscal year ended June 30, 2007, the System implemented GASB Statement No. 43, Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans. This statement provides uniform financial reporting standards for pension plans that provide postemployment benefits such as healthcare benefits. It addresses how plan administrators should account for and report their costs and obligations related to postemployment healthcare and other nonpension benefits. These benefits are collectively referred to as other postemployment benefits (OPEB).

NOTE 3 – INVESTMENTS

Investments are subject to certain types of risks, including interest rate risk, custodial credit risk, credit quality risk, foreign currency risk, and concentration of credit risk. The following describes those risks:

Interest Rate Risk – The fair value of fixed maturity investments fluctuate in response to changes in market interest rates. Increases in prevailing interest rates generally translate into decreases in fair value of those instruments. The fair value of interest sensitive instruments may also be affected by the creditworthiness of the issuer, prepayment options, relative values of alternative investments, and other general market conditions. Certain fixed maturity investments have call provisions that could result in shorter maturity periods. The System does not have a policy regarding interest rate risk. As of June 30, 2007, GNMAs in the amount of $1,049,000 and U.S. government agency securities in the amount $239,315,000 are backed by mortgage pass-throughs which are highly sensitive to interest rate changes. Therefore, if interest rates decline, the mortgages are subject to prepayment by borrowers. However, the System's intent is to hold all fixed maturity investments until maturity, and accordingly, fixed maturity investments are classified in the following tables as if they were held to maturity. International government bonds includes $532,619 of a variable rate bond linked to the URINUSCA Index that is reset semi-annually. The amount of international corporate bonds includes $2,714,646 of a principle only investment and $703,092 of a floating rate security linked to the KRW 3 months CD that is reset quarterly. As of June 30 2006, the GNMA's were in the amount of $1,321,000 and the amount for US government agency securities were $172,192,000. In addition, as of June 30, 2007 $2,298,000 of the collateralized mortgage obligations (CMO) are floating rate securities tied to the 1 to 12 month LIBOR plus 32-45 bps, and $1,495,000 of the FHMC's is a floating rate security tied to the one-year CMT plus 212.9 bps. In 2006, $4,891,000 of the CMO's tied to the 1 to 12 month LIBOR plus 31-250 bps and $2,062,000 of the FNMA's were floating rate securities tied to the one-year CMT plus 212.9 bps.

Custodial Credit Risk – Custodial credit risk is the risk that the System will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party if that outside party fails. The System's custodian holds all investments of the System in the System's nominee name except for the assets held in pooled funds, which are under custody of the investment managers' custodian bank.

Credit Quality Risk – Nationally recognized statistical rating organizations provide ratings of debt securities quality based on a variety of factors, such as the financial condition of the issuers, which provide investors with some idea of the issuer's ability to meet its obligations. The System's assets shall generally be invested in investment grade, marketable, fixed-income securities. Domestic fixed maturity investment grade shall be defined as being rated Baa/BBB or better by two of the following three rating services; Moody's Investor Services (Moody's), Standard & Poor's Corporation (S&P) or Fitch Rating Services (Fitch's). In the event that ratings are provided by only two agencies and the third is non-rated, the most conservative (lowest) rating will be assigned. If only one agency assigns a rating, that rating will be used. Up to 15% investment in BB or B securities will be permitted with written authorization of the Board. The investment managers employed to manage domestic fixed-income securities will have discretion in the day-to-day management of the funds under their control. International fixed maturity must be at least Aa3/AA-. If the corresponding ratings assigned by S&P and Moody's are not equivalent, the higher rating will be used for purposes of measuring portfolio and security quality. If a security is not rated by S&P or Moody's, the equivalent rating determined by the investment manager's research department will be used. If bonds are downgraded below the minimum credit quality allowable in the guidelines at the time of purchase, the manager is permitted to hold up to 2% of the System's portfolio managed by the individual manager, using the lower of S&P, Moody's, and Fitch's rating in the event of a split-rated security. The System may hedge against the possible adverse effects of currency fluctuations on the System's portfolio of international fixed income obligations when it is considered appropriate. Short-term investments may consist of commercial paper rated at least A1 or P1, repurchase agreements, short-term U.S. securities, and other money market investments.

Foreign Currency Risk – The risk that changes in exchange rates will adversely affect the fair value of an investment. To mitigate this risk, individual investment managers are permitted to defensively hedge currency to mitigate the impact on currency fluctuation on the underlying asset value.

Notes to Basic Financial Statements *Continued*

NOTE 3 – INVESTMENTS *Continued*

Concentration of Credit Risk – The System's investment policy limits the aggregate amount that can be invested in each class of investments. The policy limits are as follows:

Domestic Equity – Minimum 38% and maximum 48% of the fair value of the aggregate portfolio.

International Equity – Minimum 10% and maximum 20% of the fair value of the aggregate portfolio.

Domestic Bonds – Minimum 24% and maximum 34% of the aggregate portfolio.

Global Bonds – Minimum 4% and maximum 10% of the aggregate portfolio.

Private Markets – Limited to 6% of the fair value of the aggregate portfolio.

Real Estate – Minimum 3% and maximum 9% of the aggregate portfolio. Real Estate investments include a warehouse located in Northern California, and an interest in six real estate funds managed by third parties.

Short-term investments include certificates of deposit and the collective short-term investment fund, which is used for overnight investment of all excess cash in the System's funds. It is invested by the System's Custodian, and held in the System Custodian's name. This fund consists of high-grade money market instruments with short maturities, such as:

- Short-term fixed corporate and U. S. agency obligations;
- Commercial Paper;
- Certificates of Deposit;
- Repurchase agreements with major banks and U.S. government securities dealers that are collateralized by obligations of the U.S. government or a federal agency, or obligations fully guaranteed by the U.S. government or a federal agency; and
- Fully insured bank deposits.

As of June 30, 2007, the System held $186,353,000 of investments issued by the Federal National Mortgage Association (including non-USD), which represents 10.0% of its plan net assets. As of June 30, 2006, the System held $144,535,000 of investments issued by the Federal National Mortgage Association (including non-USD), which represents 8.9% of its plan net assets.

Notes to Basic Financial Statements *Continued*

NOTE 3 – INVESTMENTS *Continued*

The following tables provide information as of June 30, 2007, concerning the fair value of investments, interest rate risk, and international currency risk:

Investment Maturities at Fair Value

As of June 30, 2007
(Dollars in thousands)

	0-3 Months	3-6 Months	6 months-1 year	1-5 years	6-10 Years	More Than 10 Years	Total Fair Value	Cost
Fixed Maturity								
Domestic								
U.S. Treasury Securities	$ -	$ 10,923	$ 8,888	$ 18,759	$ -	$ 2,217	$ 40,787	$ 40,932
GNMA	-	-	-	-	-	1,049	1,049	1,078
Other U.S. Gov't Agency Securities	-	-	-	430	955	9,811	11,196	11,277
FHLMC	8,677	-	-	516	5,297	39,533	54,023	54,634
FNMA	14,638	-	-	4,378	10,531	155,746	185,293	187,777
Asset Backed Securities	-	-	-	25,387	8,440	9,494	43,321	43,406
Collateralized Mortgage Obligations	-	-	-	2,019	-	46,020	48,039	49,495
Corporate Bonds	2,070	1,639	1,243	34,005	37,197	42,755	118,909	118,227
Collective Short-Term Investments	79,751	-	-	-	-	-	79,751	79,751
Total Domestic Fixed Maturity	**105,136**	**12,562**	**10,131**	**85,494**	**62,420**	**306,625**	**582,368**	**586,577**
International								
Government Bonds								
British Pound	-	-	-	1,374	404	1,966	3,744	3,822
Canadian Dollar	-	-	-	154	1,251	-	1,405	1,361
Colombian Peso	-	-	-	152	514	95	761	633
Euro Currency	-	-	-	7,747	6,182	9,049	22,978	23,627
Japanese Yen	5,802	-	3,142	5,031	4,248	2,826	21,049	22,656
Mexican Peso	-	-	-	-	-	416	416	413
New Zealand Dollar	-	-	-	-	644	-	644	639
Norwegian Krone	-	-	-	1,008	1,264	-	2,272	2,180
Polish Zloty	-	-	-	-	1,119	-	1,119	1,104
Singapore Dollar	-	-	-	3,476	-	-	3,476	3,439
South African Rand	-	-	-	918	-	-	918	1,019
Swedish Krona	-	-	-	2,257	-	-	2,257	2,235
United States Dollar Denominated	-	-	-	-	711	1,188	1,899	1,854
Total International Government Bonds	**5,802**	**-**	**3,142**	**22,117**	**16,337**	**15,540**	**62,938**	**64,982**
Corporate Bonds								
British Pound	-	-	-	1,990	2,079	423	4,492	4,455
Canadian Dollar	-	-	-	-	719	47	766	756
Euro Currency	-	-	-	3,144	3,145	245	6,534	6,379
Iceland Krona	-	-	1,121	-	-	-	1,121	973
Indonesian Rupiah	-	-	-	422	-	-	422	378
Japanese Yen	-	-	-	5,558	2,829	1,559	9,946	10,475
Malaysian Ringgit	-	-	-	2,213	-	-	2,213	2,230
Mexican Peso	-	-	-	-	302	942	1,244	1,248
South Korean Won	-	-	-	1,504	-	-	1,504	1,398
Swiss Franc	-	-	-	1,132	-	-	1,132	1,119
United States Dollar Denominated	549	-	-	535	5,162	3,264	9,510	9,389
Total International Corporate Bonds	**549**	**-**	**1,121**	**16,498**	**14,236**	**6,480**	**38,884**	**38,800**
Total International Fixed Maturity	**6,351**	**-**	**4,263**	**38,615**	**30,573**	**22,020**	**101,822**	**103,782**
TOTAL FIXED MATURITY	**$111,487**	**$12,562**	**$14,394**	**$124,109**	**$92,993**	**$328,645**	**$684,190**	**$690,359**

Notes to Basic Financial Statements *Continued*

NOTE 3 – INVESTMENTS *Continued*

(Dollars in thousands)

Type of Investment	*Total Fair Value*	*Cost*
Equity		
Domestic	$ 371,944	$ 299,397
Pooled Domestic Equity	412,623	272,725
Total Domestic Equity	**784,567**	**572,122**
International		
Australian Dollar	8,731	5,523
Brazilian Real	4,714	3,353
British Pound	27,733	22,452
Canadian Dollar	10,827	7,628
Danish Krone	1,263	653
Euro Currency	68,905	47,044
Hong Kong Dollar	3,207	1,554
Japanese Yen	42,051	31,948
Mexican Peso	1,516	1,157
Norwegian Krone	6,771	4,629
Polish Zloty	1,213	915
Singapore Dollar	1,697	1,538
South African Rand	738	456
South Korean Won	5,816	3,329
Swedish Krona	7,257	3,910
Swiss Franc	7,940	5,891
USD Denominated	41,360	29,544
Pooled Foreign Equity	106,014	37,451
Total Foreign Equity	**347,753**	**208,975**
TOTAL EQUITIES	**1,132,320**	**781,097**
Private Equity	**26,956**	**28,289**
Real Estate	**81,332**	**69,695**
Total Private Equity and Real Estate	**108,288**	**97,984**
Forward International Currency Contracts, Net	**(41)**	**-**
Securities Lending Collateral Investment Pool*	**193,918**	**193,918**
TOTAL INVESTMENTS	**$2,118,675**	**$1,763,358**

**See Note 4*

Notes to Basic Financial Statements *Continued*

NOTE 3 – INVESTMENTS *Continued*

The following tables provide information as of June 30, 2006, concerning the fair value of investments, interest rate risk, and international currency risk:

Investment Maturities at Fair Value

As of June 30, 2006
(Dollars in thousands)

	0-3 Months	3-6 Months	6 months-1 year	1-5 years	6-10 Years	More Than 10 Years	Total Fair Value	Cost
Fixed Maturity								
Domestic								
U.S. Treasury Securities	$ (26)	$ -	$ 1,985	$ 60,672	$ -	$ 6,520	$ 69,151	$ 70,467
GNMA	-	-	-	-	-	1,321	1,321	1,365
Other U.S. Gov't Agency Securities	-	-	-	554	1,085	4,396	6,035	6,119
FHLMC	-	-	-	206	5,567	25,977	31,750	32,830
FNMA	4,162	-	7,509	2,028	15,965	110,778	140,442	143,901
Asset Backed Securities	-	-	-	27,157	3,227	8,352	38,736	39,086
Collateralized Mortgage Obligations	-	-	-	1,271	-	45,633	46,904	48,650
Corporate Bonds	450	303	1,017	38,461	39,453	35,384	115,068	116,109
Collective Short-Term Investments	26,295	-	1,383	3,163	-	-	30,841	30,860
Total Domestic Fixed Maturity	**30,881**	**303**	**11,894**	**133,512**	**65,297**	**238,361**	**480,248**	**489,387**
International								
Government Bonds								
British Pound	-	-	-	-	-	1,276	1,276	1,306
Colombian Peso	-	-	-	113	359	-	472	522
Euro Currency	2,422	-	-	12,414	7,669	7,432	29,937	31,117
Japanese Yen	-	975	-	15,002	3,283	-	19,260	20,271
Mexican Peso	-	-	-	-	1,980	148	2,128	2,132
New Zealand Dollar	-	-	-	-	754	-	754	882
Norwegian Krone	-	-	-	968	-	-	968	908
Singapore Dollar	-	-	2,201	836	-	-	3,037	3,055
South African Rand	-	-	-	947	-	-	947	1,019
Swedish Krona	-	-	-	3,007	-	-	3,007	3,196
United States Dollar Denominated	-	-	-	-	253	2,551	2,804	2,691
Total International Government Bonds	**2,422**	**975**	**2,201**	**33,287**	**14,298**	**11,407**	**64,590**	**67,099**
Corporate Bonds								
Austrailian Dollar	-	-	-	458	458	-	916	973
Brazilian Real	-	-	-	488	-	-	488	383
British Pound	-	-	-	1,854	1,430	813	4,097	4,215
Canadian Dollar	-	-	-	-	891	-	891	891
Euro Currency	-	-	457	3,011	3,815	-	7,283	7,565
Indonesian Rupiah	-	-	-	419	-	-	419	378
Japanese Yen	-	-	-	9,621	-	-	9,621	10,573
Mexican Peso	-	-	-	-	301	-	301	321
New Zealand Dollar	-	-	-	430	113	-	543	643
South Korean Won	-	-	-	1,460	-	-	1,460	1,398
Thai Bhat	-	-	-	973	-	-	973	930
United States Dollar Denominated	-	-	-	2,325	4,973	2,519	9,817	10,105
Total International Corporate Bonds	**-**	**-**	**457**	**21,039**	**11,981**	**3,332**	**36,809**	**38,375**
Total International Fixed Maturity	**2,422**	**975**	**2,658**	**54,326**	**26,279**	**14,739**	**101,399**	**105,474**
TOTAL FIXED MATURITY	**$33,303**	**$1,278**	**$14,552**	**$187,838**	**$91,576**	**$253,100**	**$581,647**	**$594,861**

Notes to Basic Financial Statements *Continued*

NOTE 3 – INVESTMENTS *Continued*

(Dollars in thousands)

Type of Investment	*Total Fair Value*	*Cost*
Equity		
Domestic	$ 343,927	$ 302,303
Pooled Domestic Equity	362,225	287,750
Total Domestic Equity	**706,152**	**590,053**
International		
Australian Dollar	6,563	5,474
Brazilian Real	3,508	3,817
British Pound	22,046	18,574
Canadian Dollar	11,976	10,023
Danish Krone	618	507
Euro Currency	57,024	45,603
Hong Kong Dollar	2,053	1,701
Hungarian Florint	1,307	1,480
Japanese Yen	43,477	34,677
Mexican Peso	1,530	1,393
Norwegian Krone	7,536	5,955
Polish Zloty	823	964
South African Rand	4,211	3,935
South Korean Won	9,493	8,233
Swedish Krona	4,160	3,202
Swiss Franc	8,584	6,966
USD Denominated	7,833	5,330
Pooled Foreign Equity	99,311	43,368
Total Foreign Equity	**292,053**	**201,202**
TOTAL EQUITIES	**998,205**	**791,255**
Private Equity	**7,956**	**8,674**
Real Estate	**54,584**	**47,821**
Total Private Equity and Real Estate	**62,540**	**56,495**
Forward International Currency Contracts, Net	**59**	**-**
Securities Lending Collateral Investment Pool*	**148,037**	**148,037**
TOTAL INVESTMENTS	**$1,790,488**	**$1,590,648**

**See Note 4*

Notes to Basic Financial Statements *Continued*

NOTE 3 – INVESTMENTS *Continued*

The following table provides information as of June 30, 2007 concerning credit risk:

Ratings of Fixed Maturities for June 30, 2007 *(Dollars in thousands)*

S&P Quality Rating	*Fair Value*	*Fair Value as a Percentage of Total Fixed Maturity*
Unrated Agency	$248,546	36.3%
AAA	180,984	26.5%
AA	27,792	4.1%
A	37,170	5.4%
BBB	45,018	6.5%
BB	20,707	3.0%
B	16,186	2.4%
CCC & Below	5	0.0%
Unrated*	107,782	15.8%
TOTAL	$684,190	100.0%

** Includes Collective Short-Term Investment Fund*

The following table provides information as of June 30, 2006 concerning credit risk:

Ratings of Fixed Maturities for June 30, 2006 *(Dollars in thousands)*

S&P Quality Rating	*Fair Value*	*Fair Value as a Percentage of Total Fixed Maturity*
Unrated Agency	$175,597	30.2%
AAA	205,356	35.3%
AA	25,506	4.4%
A	41,756	7.2%
BBB	42,594	7.3%
BB	27,590	4.7%
B	10,250	1.8%
CCC & Below	-	0.0%
Unrated*	52,998	9.1%
TOTAL	**$581,647**	**100.0%**

**Includes Collective Short-Term Investment Fund*

International Forward Currency Contracts - The System has made investments in forward currency contracts, which are commitments to purchase or sell stated amounts of international currency. The System utilizes these contracts to control exposure and facilitate the settlement of international security purchase and sale transactions. At June 30, 2007 and 2006, the System's net position in these contracts is recorded at fair value as international forward currency contracts. The fair values of forward currency contracts are determined by quoted currency prices from national exchanges. The System's investments in forward currency contracts bear credit risk in that parties to the contracts may fail to perform according to the terms of the contract. As of June 30, 2007, total commitments in forward currency contracts to purchase and sell international currencies were $10,008,000 and $10,008,000, respectively, with market values of $10,003,000 and $10,044,000 respectively. As of June 30, 2006, total commitments in forward currency contracts to purchase and sell international currencies were $10,821,000 and $10,821,000, respectively, with market values of $10,867,000 and $10,808,000, respectively. The System's commitments relating to forward currency contracts are settled on a net basis. The Systems's investments in forward currency contracts bear credit risk in that parties to the contracts may fail to perform according to the terms of the contract. As of June 30, 2007, total commitments in forward currency contracts to purchase and sell international currencies were $4,974,000 and $4,974,000 respectively, with fair values of $4,948,000 and $4,981,000, respectively. As of June 30, 2006, the System had commitments in international currency contracts to purchase and sell international currencies of $1,496,000 and $1,496,000, respectively, with fair values of $1,505,000 and $1,497,000, respectively. The System's commitments relating to forward currency contracts are settled on a net basis.

NOTE 4 – SECURITIES LENDING PROGRAM

The San José municipal code and the investment policy, adopted by the Board, permit the use of a securities lending program with its principal custodian bank. The System does not have a threshold for securities lending. (The investment policy requires that loan maturities cannot stretch beyond one year, and no more than 15% of the portfolio can be lent longer than six months.) The System has a custodial agreement with the Northern Trust Company, which authorizes the Northern Trust Company to loan securities in the System's investment portfolio under such terms and conditions as the Northern Trust Company deems advisable and to permit the loaned securities to be transferred into the name of the borrowers. The System receives a fee from the borrower for the use of the loaned securities. If the loaned securities are not returned by the borrower, the Northern Trust Company is responsible for replacement of the loaned securities with other securities of the same issuer, class and denomination, or if such securities are not available on the open market, the Northern Trust Company is required to credit the System's account with the market value of such unreturned loaned securities. All securities loan agreements can be terminated on demand within a period specified in each agreement by either the System or borrowers.

Securities lending collateral represents investments purchased with cash collateral, as well as securities collateral that may be pledged or sold without a default by the borrower. Securities lending collateralized with securities that cannot be pledged or sold without borrower default are not reported as assets and liabilities in the statement of net assets. The System does not match the maturities of investments made with cash collateral with the securities on loan.

Notes to Basic Financial Statements *Continued*

NOTE 4 – SECURITIES LENDING PROGRAM *Continued*

The System authorized The Northern Trust Company to invest and reinvest cash collateral in Northern Trust's pooled investment vehicle which must have weighted average life of 60 days or less. Securities with maturities of 13 months or more must have a rating of A or better. Securities with maturities of less than 13 months are rated at least A-1/P-1. As of June 30, 2007, the size of the cash collateral pooled vehicle was $95.7 billion with a weighted average life of 39 days. The cash collateral investments included time deposits (12% of the pool), repurchase agreements (21%), asset backed securities (16%), certificates of deposit (14%), variable rate securities (14%), commercial paper (19%) and other bank notes (4%). As of June 30, 2006, the size of the cash collateral pooled vehicle was $85.9 billion and the weighted average life was 41 days. The cash collateral investments included time deposits (19% of the pool), repurchase agreements (18%), asset backed securities (17%), certificates of deposit (15%), variable rate securities (14%) and other bank notes (2%). All of the underlying investments of the System's securities lending cash collateral are held by the counterparty, not in the name of the System.

The loaned securities as of June 30, 2007 and 2006, consisted of U.S. Treasury securities, U.S. government agency securities, international government bonds, domestic corporate bonds, domestic equity securities, and international equity securities and international corporate bonds. In return, the System receives collateral in the form of cash or securities equal to at least 102% of the transferred securities plus accrued interest for reinvestment.

As of June 30, 2007, the underlying securities loaned by the System as a whole amounted to approximately $194,984,000. The cash collateral and the non-cash collateral totaled $193,918,000 and $5,904,000, respectively. As of June 30, 2006, the underlying securities loaned by the System as a whole amounted to approximately $163,839,000. The cash collateral and the non-cash collateral totaled $148,037,000 and $18,573,000, respectively. The System has no exposure to credit risk related to the securities lending transactions as of June 30, 2007 and 2006.

Securities Lending – Investment and Collateral Received

(At Fair Value in Thousands)

Type of Investment Lent	*2007*	*2006*
For Cash Collateral		
U.S. government and agencies	$ 130	$ -
Domestic corporate bonds	20,921	17,909
Domestic equity securities	103,041	74,262
U.S. treasury notes and bonds	39,919	30,551
International government bonds	3,239	2,558
International equity securities	21,600	20,295
International corporate bonds	337	-
Total Lent for Cash Collateral	**$189,187**	**$145,575**
For Non-Cash Collateral		
Domestic corporate bonds	2,196	1,940
Domestic equity securities	1,648	2,314
U.S. treasury notes and bonds	835	13,614
International equity securities	1,118	396
Total Lent for Non-Cash Collateral	**5,797**	**18,264**
TOTAL SECURITIES LENT	**$194,984**	**$163,839**

Type of Collateral Received	*2007*	*2006*
Cash Collateral	**$193,918**	**$148,037**
Non-Cash Collateral		
For lent domestic corporate bonds	2,181	1,972
For lent domestic equity securities	1,694	2,355
U.S. treasury notes and bonds	853	13,834
For lent international equity securities	1,176	412
Total Non-Cash Collateral	**5,904**	**18,573**
TOTAL COLLATERAL RECEIVED	**$199,822**	**$166,610**

Notes to Basic Financial Statements *Continued*

NOTE 4 – SECURITIES LENDING PROGRAM *Continued*

As of June 30, 2007 the fair value of the collateral provided was 102.48% of the fair value of the investment lent, thus meeting the System's policy of 102%. As of June 30, 2006 the fair value of the collateral provided was 101.67% of the fair value of the investments lent, thus did not meet the System's policy of 102% due to daily market fluctuations on the securities lent. The custodian marks to market the securities on loan at the end of the day and cash collateral for those securities are settled at the beginning of the next business day. As of July 3, 2006 the fair value of collateral was 102.03% of the fair value of investments lent.

NOTE 5 – DEFINED BENEFIT PENSION PLAN CONTRIBUTIONS AND FUNDING POLICY

Contributions to the Defined Benefit Pension Plan for both the City and the participating employees are based upon an actuarially determined percentage of each employee's base salary sufficient to provide adequate assets to pay benefits when due. The significant actuarial assumptions used to compute the actuarially determined contribution requirement are the same as those used to compute the actuarial accrued liability shown in the Schedule of Funding Progress for the Defined Benefit Pension Plan (see page 37).

The City and the participating employee contribution rates in effect during the fiscal years ended June 30, 2007 and 2006, were as follows:

Period	*City*	*Employee*
7/2/06 – 6/30/07	18.16%	4.26%
7/1/05 – 7/1/06	14.96%	4.26%

NOTE 6 – DEFINED POSTEMPLOYMENT HEALTHCARE BENEFIT PLAN CONTRIBUTIONS, FUNDED STATUS AND FUNDING PROGRESS

Contributions – Contributions to the Defined Postemployment Healthcare Plan are made by both the City and the participating employees. Contributions for the fiscal years ended June 30, 2007 and 2006, are based upon an actuarially determined percentage of each employee's base salary prior to the requirements of GASB Statement No. 43. The contributions are not sufficient to provide adequate assets to pay benefits when due in accordance with the requirements of GASB Statement No. 43. Contributions to the Defined Postemployment Healthcare Plan for both the City and the participating employees are based upon an actuarially determined percentage of each employee's base salary sufficient to provide adequate assets to pay benefits when due. The City and the participating employee contribution rates in effect during the fiscal years ended June 30, 2007 and 2006 for the Defined Postemployment Healthcare Benefit Plan were as follows:

Period	*City*	*Employee*
7/2/06 – 6/30/07	3.82%	3.32%
7/1/05 – 7/1/06	2.16%	1.80%

The funding status of the Defined Postemployment Healthcare Plan as of June 30, 2006, the most recent actuarial valuation date, is as follows:

(Dollars in thousands)

Acturial Valuation Date	*Actuarial Value of Assets (a)*	*Actuarial Accrued Liability (AAL) (b)*	*Unfunded (Overfunded) AAL (UAAL) (b-a)*	*Funded Ratio (a)/(b)*	*Annual Covered Payroll (c)*	*UAAL as a % of Covered Payroll ((b)-(a)/(c))*
6/30/06	$81,288	$702,939	$621,651	12%	$275,559	226%

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Actuarially determined amounts are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

Projections of benefits for financial reporting purposes are based on the substantive plan in effect and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

Notes to Basic Financial Statements *Continued*

NOTE 6 – DEFINED POSTEMPLOYMENT HEALTHCARE BENEFIT PLAN CONTRIBUTIONS, FUNDED STATUS AND FUNDING PROGRESS *Continued*

The significant actuarial methods and assumptions used to compute the actuarially determined annual required contribution are as follows:

Description	*Method/Assumption*
Valuation Date	June 30, 2006
Actuarial Cost Method	Entry age normal cost method
Amortization Method	Level percentage of payroll
Remaining Amortization Period	30 years, open
Actuarial Asset Valuation Method	5 year smoothed market
Actuarial Assumptions:	
Discount rate	5.6%*
Inflation rate	4.0%
Projected payroll increases	4.25
Health Care Cost Trend Rate:	
Medical	The valuation assumes that future medical inflation will be at a rate of 12% per annum graded down each year in 1% increments to an ultimate rate of 4%.
Dental	Dental inflation is assumed to be 6% graded down to 4% over a nine year period.

**Determined as a blended rate of the expected long-term investment returns on plan assets and on the City's investments, based on the funded level of the plan at the valuation date.*

The schedules presented as required supplementary information following the notes to the financial statements, present multi-year trend information. The Schedule of Funding Progress for the Defined Postemployment Healthcare Benefit Plan presents information about whether the actuarial values of plan assets are increasing or decreasing over time relative to the actuarial accrued liabilities for benefits. The Schedule of Employer Contributions for the Defined Postemployment Healthcare Benefit Plan presents trend information about the amounts contributed to the plan by employers in comparison to the annual required contribution (ARC) determined in accordance with the parameters of GASB Statement 43. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost for each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years.

Required Supplementary Information

SCHEDULE OF FUNDING PROGRESS - DEFINED BENEFIT PENSION PLAN (Unaudited)

(Dollars in thousands)

Acturial Valuation Date	*Actuarial Value of Assets[(a)]*	*Actuarial Accrued Liability (AAL)*	*Unfunded AAAL*	*Funded Ratio*	*Annual Covered Payroll [(b)]*	*Unfunded AAL as a % of Annual Covered Payroll*
June 30, 1999	804,860	862,226	57,366	93%	196,178	29%
June 30, 2001	1,060,144	1,072,333	12,189	99%	252,696	5%
June 30, 2003	1,280,719	1,311,691	30,972	98%	292,961	11%
June 30, 2005	1,384,454	1,711,370	326,916	81%	286,446	114%

Actuarial valuations have been performed bi-annually through June 30, 2005.

(a) Reported at "smoothed market" value determined using a technique that smoothes the effect of short-term volatility in the market value of investments over a five-year period.

(b) Annual covered payroll represents the actuarial estimate of annual covered payroll for the subsequent year.

SCHEDULE OF EMPLOYER CONTRIBUTIONS - DEFINED BENEFIT PENSION PLAN (Unaudited)

(Dollars in thousands)

Fiscal Year Ended June 30,	*Annual Required Employer Contributions*	*Percentage Contributed*
2002	$ 41,011	100%
2003	38,411	100%
2004	39,534	100%
2005	41,552	100%
2006	41,267	100%
2007	51,004	100%

Required Supplementary Information *Continued*

SCHEDULE OF ACTUARIAL METHODS AND ASSUMPTIONS - DEFINED BENEFIT PENSION PLAN (Unaudited)

For Fiscal Year Ended June 30, 2007

Description	*Method/Assumption*
Valuation date	June 30, 2005
Actuarial cost method	Entry age normal cost method
Amortization method for actuarial accrued liabilities	Level percentage of payroll
Remaining amortization period	30 years, open
Actuarial asset valuation method	5 year smoothed market
Actuarial assumptions:	
Assumed rate of return on investments	8.25% per annum
Postretirement mortality	The 1994 Group Annuity Mortality Table was used for healthy retirees and beneficiaries. The disabled mortality table used was the 1981 Disability Mortality Table.
Active service, withdrawal, death, disability service retirement	Tables based on current experience
Salary increases	The rate of annual salary increase for all members with at least 5 years of service is equal to 4.25% plus an added merit component for those with 0-4 years of service.
Cost-of-living adjustments	3.00% a year

POSTEMPLOYMENT HEALTHCARE BENEFIT PLAN (Unaudited)

For the Fiscal Year Ended June 30, 2007

(Dollars in thousands)

Schedule of Funding Progress

Acturial Valuation Date	*Actuarial Value of Assets (a)*	*Actuarial Accrued Liability (AAL) (b)*	*Unfunded (Overfunded) AAL (UAAL) (b-a)*	*Funded Ratio (a)/(b)*	*Annual Covered Payroll (c)*	*UAAL as a % of Covered Payroll ((b)-(a)/c))*
June 30, 2006	$81,288	$702,939	$621,651	12%	$275,559	226%

Schedule of Employer Contributions

Plan Year Beginning	*Annual Required Contributions*	*Actual Contributions*	*Percentage Contributed*
June 30, 2006	$38,526	$10,728	28%

Other Supplementary Information

COMBINING SCHEDULE OF DEFINED BENEFIT PENSION PLAN NET ASSETS

June 30, 2007

(Dollars in thousands)	*Retirement Fund*	*Cost-of-Living Fund*	*Total*
ASSETS			
Receivables:			
Employee contributions	$ 360	$ 106	$ 466
Employer contributions	1,566	468	2,034
Brokers and others	66,773	22,257	89,030
Accrued investment income	4,811	1,578	6,389
Total receivables	**73,510**	**24,409**	**97,919**
Investments, at fair value:			
Securities and Other:			
U.S. Treasury notes and bonds	28,600	10,085	38,685
U.S. government agency securities	176,395	62,199	238,594
International government bonds	44,132	15,562	59,694
Domestic corporate bonds	147,442	51,990	199,432
International corporate bonds	27,266	9,614	36,880
Domestic equity securities	550,141	193,988	744,129
International equity securities	243,846	85,983	329,829
Private market equity	18,902	6,665	25,567
International forward currency contracts	(29)	(10)	(39)
Collective short-term investment funds	55,923	19,718	75,641
Real estate	57,030	20,110	77,140
Securities lending cash collateral investment pool	137,843	45,943	183,786
Total investments	**1,487,491**	**521,847**	**2,009,338**
TOTAL ASSETS	**1,561,001**	**546,256**	**2,107,257**
LIABILITIES			
Payable to brokers	116,650	38,879	155,529
Securities lending collateral due to borrowers	137,843	45,943	183,786
Other liabilities	1,172	373	1,545
TOTAL LIABILITIES	**255,665**	**85,195**	**340,860**
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS	**$1,305,336**	**$461,061**	**$1,766,397**

Other Supplementary Information *Continued*

COMBINING SCHEDULE OF CHANGES IN DEFINED BENEFIT PENSION PLAN NET ASSETS

For the Fiscal Year Ended June 30, 2007

(Dollars in thousands)	*Retirement Fund*	*Cost-of-Living Fund*	*Total*
ADDITIONS			
Contributions:			
Employee	$ 9,525	$ 2,845	$ 12,370
Employer	39,262	11,742	51,004
Total Contributions	**48,787**	**14,587**	**63,374**
Investment income:			
Net appreciation in fair value of investments	155,970	51,736	207,706
Interest income	22,669	7,535	30,204
Dividend income	6,327	2,102	8,429
Net rental income	2,911	969	3,880
Less investment expense	(4,850)	(1,639)	(6,489)
Net investment income before securities lending income	**183,027**	**60,703**	**243,730**
Securities lending income:			
Earnings	7,232	2,402	9,634
Rebates	(6,752)	(2,242)	(8,994)
Fees	(120)	(40)	(160)
Net securities lending income	**360**	**120**	**480**
Total investment income	**183,387**	**60,823**	**244,210**
TOTAL ADDITIONS	**232,174**	**75,410**	**307,584**
DEDUCTIONS			
Retirement benefits	60,438	14,697	75,135
Death benefits	3,634	2,233	5,867
Refund of contributions	813	195	1,008
Administrative expenses and other	1,439	406	1,845
TOTAL DEDUCTIONS	**66,324**	**17,531**	**83,855**
Net increase	165,850	57,879	223,729
PLAN NET ASSETS HELD IN TRUST FOR			
Pension benefits:			
BEGINNING OF YEAR	**1,139,486**	**403,182**	**1,542,668**
END OF YEAR	**$1,305,336**	**$461,061**	**$1,766,397**

Other Supplementary Information *Continued*

SCHEDULES OF ADMINISTRATIVE EXPENSES AND OTHER

For the Fiscal Years Ended June 30, 2007 and 2006

	2007			2006
	Original Budget	*Actual*	*Variance Positive/(Negative)*	*Actual*
Personal services	$ 1,593,284	$ 1,420,617	$ 172,667	$ 1,269,137
Non-personal/equipment	596,800	403,707	193,093	445,280
Professional services	187,349	125,226	62,123	179,025
TOTAL ADMINISTRATIVE EXPENSES AND OTHER	**$2,377,433**	**$1,949,550**	**$427,883**	**$1,893,442**

SCHEDULES OF INVESTMENT EXPENSES

For the Fiscal Years Ended June 30, 2007 and 2006

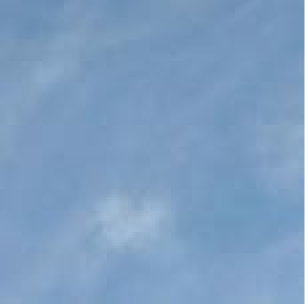
	2007	2006
Equity:		
Domestic equity	$1,911,549	$1,724,281
International equity	1,772,220	1,718,023
Private equity	741,982	-
Total equity	**4,425,751**	**3,442,304**
Fixed income:		
Domestic fixed income	919,340	863,208
Global fixed income	372,912	341,659
Total fixed income	**1,292,252**	**1,204,867**
Real estate	993,413	340,641
Total investment managers' fees	**6,711,416**	**4,987,812**
Other investment service fees:		
Investment consultant	120,000	100,000
Proxy voting	3,900	6,100
Real estate legal fees	449	3,753
Real estate appraisal	-	5,250
Custodian	5,855	128,129
Total other investment service fees	**130,204**	**243,232**
TOTAL INVESTMENT EXPENSES	**$6,841,620**	**$5,231,044**

Other Supplementary Information *Continued*

SCHEDULES OF PAYMENTS TO CONSULTANTS

For the Fiscal Years Ended June 30, 2007 and 2006

Firm	*Nature of Service*	*2007*	*2006*
Levi, Ray & Shoup	Web Development, Maintenance and Hosting	$ 17,595	$ 15,463
Levi, Ray & Shoup	Document Imaging & Support and Maintenance	7,665	7,500
Macias Gini & O'Connell LLP	External Auditors	32,008	31,380
Avery, William, & Associate	Human Resource Consultant	-	12,200
Medical Director/Other Medical	Medical Consultant	26,191	29,709
Pension Benefit Information	Reports on Beneficiary Deaths	3,146	2,261
Saltzman & Johnson	Legal Counsel	9,871	12,557
Gabriel, Roeder, Smith & Company	Actuarial Consultant	28,750	67,955
TOTAL		**$125,226**	**$179,025**



Investment Section

Report on Investment Activity

Northern Trust

The Northern Trust Company
50 South La Salle Street
Chicago, IL 60603

312.630.600 phone
www.northerntrust.com

August 20, 2007

Mr. Edward Overton
Director of Retirement Services
Federated City Employees' Retirement System
1737 North First Street, Suite 580
San Jose, CA 95112-4505

Dear Mr. Overton:

The information contained within this letter includes a review of investment performance results for the Federated City Employees' Retirement System of San Jose covering the fiscal year ending June 30, 2007 as well as a summary of financial markets activity during the aforementioned time period.

Background

The objectives of the System have been established in conjunction with a comprehensive review of the current and projected financial requirements. The Board ensures that appropriate investment managers and other professionals will be employed to assist in achieving financial goals.

The Northern Trust Company, global custodian for the System, provides quarterly investment performance reviews based on plan accounting information. Northern Trust calculates rates of return and other measures in accordance with CFA Institute, GIPS and BAI standards.

Financial Markets Review

The fiscal year ending June 30, 2007 marked a slowdown within the US economy as oil prices continued to rise while the housing market cooled significantly. The Fed left short-term interest rates unchanged at 5.25% during the year ending 6/30/07.

U.S. Equities boasted double-digit returns across many sectors including value-oriented issues during the fiscal year ending June 30, 2007. Value issues (which generally comprise cyclical sectors such as materials, industrials and utilities) continued the trend of outperforming their growth counterparts (i.e. information technology, consumer goods, etc.) over the aforementioned one year period. Small cap stocks produced returns on par with their larger capitalization counterparts for the year ending 6/30/07.

Fixed Income markets rebounded during the year ending June 30, 2007 as the Federal Reserve Bank maintained the general level of short-term interest rates. Increased merger & acquisition activity combined with significant demand within the leveraged buyout space drove double-digit returns across high yield issues.

Report on Investment Activity *Continued*

Northern Trust

International Equity markets, boosted by value sectors such as materials, utilities and industrials produced very strong results during the fiscal year ending June 30, 2007. Major contributors to overseas performance (on a weighted country basis) came from the United Kingdom which provided a 27.45% return and Germany, which provided a 49.58% return for the one year period ending June 30, 2007.**

***All returns expressed in U.S. Dollar terms.*

Investment Results

Investment performance for the Federated City Employees' Retirement System of San Jose was strong in absolute terms during the fiscal year ending June 30, 2007 as well as on a relative basis versus metrics including the actuarial assumption rate (8.25%), passive management alternatives and peer group comparisons. Specifically, the system produced a return of 16.22% over the one year period, 11.74% over three years and 11.78% over the five years ending 6/30/07.

Peer group comparisons are based using Wilshire's Trust Universe Comparison Service (TUCS). TUCS is a cooperative effort among custodial banks and Wilshire Associates whereby custodians submit asset positions and performance information to Wilshire, which is then aggregated into various universes for comparison purposes. The Northern Trust Company maintains a membership in TUCS and provides clients TUCS data as an option with the performance measurement service.

For the System, comparisons at the total fund level are made versus several peer universes including TUCS' Public Fund Universe. As of 6/30/07, the System's one year return ranked in the 48th percentile (1st percentile being the highest, 99th percentile being the lowest) relative to peers within the Public Fund space. Longer term returns were comparatively strong as the four, five and seven year rankings of 43rd percentile, 26th percentile and 6th percentile respectively, indicate.

The System's asset allocation employs a diversified mix of stocks, bonds, real estate and cash invested within the U.S. as well as across markets around the globe. Within the domestic equity strategy, the System implements a "core/satellite" approach in which the majority of assets are indexed to a broad-based, investable universe of stocks, (specifically, the Russell 3000 Index) and then "satellites" around this component employing investment managers which specialize across large and small capitalization issues as well as across growth/value investment styles.

In addition to the inclusion of publicly traded equities, the System's level of invested capital into private equity vehicles increased during the fiscal year ending June 30, 2007. Private equity investment can offer the potential for higher rate-of-return opportunities as access is made available to the universe of privately held

Report on Investment Activity *Continued*

Northern Trust

companies, generally not available for investment through traditional means. Furthermore, private equity partnerships can often influence the operations and management of the invested companies, thus allowing for higher return prospects.

International equity investments have been accessed through investment managers who proxy their performance versus the Morgan Stanley All Country World (Ex-United States) Index (MS ACWI Ex-U.S.). Overseas equity markets demonstrated considerable strength during the year ending June 30, 2007 as global economy expansion combined with a weak U.S. Dollar pushed returns higher. Most developed and emerging European and Asian countries within the index posted 20+ % returns during the year ending 6/30/07 (with the exception of Japan) with the majority returning in excess of 30%.

Fixed Income assets can provide stability in that cash flows are more predictable and price movements are generally less volatile than equities. The System invests in bond instruments within the United States and internationally using a multiple investment manager platform.

The System's Real Estate portfolio increased as a percentage of the total fund over the year ending June 30, 2007. Real Estate properties, primarily accessed through commingled fund vehicles, have provided significant benefit over short and longer-term periods as cash flows and market appreciation from property holdings have resulted in double-digit returns over the one, three and five years ending June 30, 2007. System assets are well diversified across retail, industrial and residential properties and further allocated regionally across the United States.

In sum, the Federated City Employees' Retirement System of San Jose continues to position its investment portfolio in order to maximize the opportunity for long-term returns while managing risk in accordance with investment objectives as outlined in the plan's Statement of Investment Policy.

Sincerely,

Steven R. Pines
Senior Investment Consultant
Investment Risk & Analytical Services

Statement of Investment Policy

The purpose of this Investment Policy Statement (IPS) is to assist the San Jose Federated City Employees' Retirement System's Board ("Board") and its delegate in effectively supervising, monitoring and evaluating the investment of the System's assets.

The System's investment program is defined in the various sections of the IPS by:

- Stating in a written document the Board's attitudes, expectations, objectives and guidelines for the investment of all the System's assets.
- Setting forth an investment structure for managing all the System's assets. This structure includes various asset classes, investment management styles, asset allocation and acceptable ranges that, in total, are expected to produce a sufficient level of overall diversification and total investment return over the long-term.
- Providing guidelines for the investment System that control the level of overall risk and liquidity assumed in that System, so that all the System's assets are managed in accordance with stated objectives.
- Encouraging effective communications between the Board, the investment consultant(s) and the money managers.
- Establishing formalized criteria to monitor, evaluate and compare the performance results achieved by the money managers on a quarterly basis, or as deemed appropriate.
- Complying with all applicable fiduciary, prudence and due diligence requirements that experienced investment professionals would utilize, and with all applicable laws, rules and regulations from various local, state, federal and international political entities that may impact the System's assets.

This IPS has been formulated, based upon consideration by the Board of the financial implications of a wide range of policies, and describes the prudent investment process that the Board deems appropriate. Highlights of the IPS are outlined below:

The objectives of the System have been established in conjunction with a comprehensive review of the current and projected financial requirements. The Board shall:

(1) Require that the Retirement System be sufficiently funded to assure that all disbursement obligations will be met.

(2) Attempt to insure that the investment earnings be sufficiently high to provide a funding source, along with contributions from City employees and the City, in order to offset liabilities in perpetuity.

(3) Strive for the highest total return on investment funds consistent with safety in accordance with accepted investment practices and maintain an appropriate asset allocation policy that is compatible with the objectives of the System.

(4) Control costs of administering the System's assets and managing the investments.

(5) Outperform passively managed portfolio invested in the proportions described in the Plan's Asset Allocation targets

(6) Perform in the top 50% of a broad universe of Public Pension Plans.

Asset Allocation Policy

The following policy has been identified by the Board as having the greatest expected investment return and the resulting positive impact on asset values and funded status without exceeding a prudent level of risk. The Board determined this policy after evaluating the implications of increased investment return versus increased variability of return for a number of potential investment policies with varying commitments to stocks and bonds.

It shall be the Policy of the System to invest its assets in accordance with the maximum and minimum range, valued at market value, for each asset class as stated below:

ASSET ALLOCATION WITHOUT PRIVATE MARKETS

Asset Class	*Minimum*	*Target*	*Maximum*
Domestic Equity	38%	43%	48%
International Equity	10%	15%	20%
Domestic Bonds	24%	29%	34%
Global Bonds	4%	7%	10%
Real Estate	3%	6%	9%

The Board approved to continue using asset allocation targets "without Private Markets" until the completion of the new Asset Liability Modeling ("ALM") study initiated this year.

ASSET ALLOCATION WITH PRIVATE MARKETS

Asset Class	*Minimum*	*Target*	*Maximum*
Domestic Equity	30%	35%	40%
International Equity	10%	15%	20%
Domestic Bonds	29%	34%	39%
Global Bonds	4%	7%	10%
Real Estate	3%	6%	9%
Private Markets	0%	3%	6%

The investment policy is expected to have a high likelihood of meeting the objectives outlined in the "Statement of Investment Objectives" section which preceded this section.

(Procedure 620.2)
The Investment Policy, including asset allocation, is intended to provide a means for controlling the overall risk of the portfolio while ensuring that investment earnings will be sufficiently high to provide a funding source to offset liabilities in perpetuity. The

Statement of Investment Policy *Continued*

policy should not unduly constrain the discretionary, tactical decision-making process of the investment managers so that the funds earn the highest total returns while remaining in accordance with accepted investment practices.

The Investment Policy and the strategic asset allocation are determined using certain capital market assumptions. These assumptions include the expected median return and standard deviation for each asset category and the expected correlation coefficients among the asset classes. When these presumptions change materially, the policy needs to be modified to compensate for those changes so that the Retirement System remains sufficiently funded to meet all distribution needs.

Time Horizon

The asset allocation ranges established by this investment policy represent the long-term perspective. As such, rapid unanticipated market shifts or changes in economic conditions may cause the asset mix to fall outside the policy range. These divergences should be of a short-term nature. The Director of Retirement Services will review the asset mix of the Plan on a semi-monthly basis and cause the asset mix to be rebalanced to within the policy range as necessary and in accordance with the rebalancing guidelines set forth in Procedure 620.3-F. Additionally, the Board will review the strategic asset allocation on an annual basis to determine if there is a need to make any changes. A formal asset liability study will be conducted every 3 to 5 years.

Risk Tolerances and Volatility

The Board recognizes the difficulty of achieving the System's investment objectives in light of the uncertainties and complexities of contemporary investment markets. The Board also recognizes that some risk must be assumed to achieve the System's long-term investment objectives.

In establishing the risk tolerances of the IPS, the ability to withstand short and intermediate term variability were considered.

Rebalancing of Strategic Allocation

(Procedure 620.3-F)

The Plan's asset allocation will be reviewed relative to the targets on a semi-monthly basis and action will be taken to rebalance to within the target ranges by means of asset transfers among the categories.

When necessary and/or available, cash inflows/outflows will be deployed in a manner consistent with the strategic asset allocation of the System.

General guidelines for rebalancing the portfolio are as follows:

1) When the allocation to a particular asset class reaches 95-100% of the maximum or 100-105% of the minimum, the fund will be rebalanced to the target over the following 60 days. The cash surplus within the Fund will be used to rebalance the portfolios. **If the cash surplus is not sufficient, the following rebalancing procedures shall be implemented.**

a) Transfers shall first be taken from asset classes above the maximum range, then from asset classes above the target but below the maximum. If there is only one manager in the asset class, transferred assets shall first consist of cash in the portfolio. If the cash is not sufficient, then the manager will be requested to liquidate that portion of the portfolio which will result in the manager's portfolio coming within the specific target range.

b) Transfers shall first be made to asset classes below the minimums, then to asset classes below the targets, unless the managers in those classes are already holding excess cash or they feel it would be imprudent to increase their size.

c) Transfers to or from the Domestic Stock asset class should be made such that the asset class remains style neutral. The portfolio should remain biased towards large capitalization over small capitalization. Transferred assets shall first consist of cash in the portfolios. If the cash is not sufficient, then the managers will be requested to liquidate that portion of the portfolios which will result in the asset class coming within the specific target range and remaining balanced between Growth and Value.

d) Since the Domestic Equity Class represents a large part of the Fund, it can be balanced internally through the use of secondary targets established within the class. The table below provides an example of how balances within the class are maintained. To determine whether the target is met for each of these categories, a subtotal is computed for the assets held by each group of managers. The percentage of the total portfolio that each group represents is determined, and compared against the target levels. When the allowable variation is exceeded, the procedures for adjustments between asset classes are then applied within the domestic equities class to meet the secondary target levels.

ASSET ALLOCATION MODEL SECONDARY TARGETS, DOMESTIC EQUITIES

Portfolio Category: Form of Investment Management	*As a % of Domestic Equity Portfolio*	*As the Equivalent % of the Total Portfolio*	*Allowable Variation from the % of the Equity Portfolio*
Index Fund	50%	17.4%	+/- 4.5%
Large Cap Value	12%	3.4%	+/- 2.5%
Large Cap Growth	10%	2.9%	+/- 2.5%
Small Cap Value	7%	3.6%	+/- 1.5%
Small Cap Growth	6%	3.1%	+/- 1.5%
All Cap Growth	15%	4.4%	+/- 2.5%

Statement of Investment Policy *Continued*

2) All transfers should be made in accordance with the cash management policy.
3) The less liquid Real Estate and Private Equity investment will be treated separately for purposes of rebalancing in order not to force liquidation of holdings.

Liquidity

The Board has authorized the Director of Retirement Services to review the projected cash flow needs of the System at least annually and indicate to the investment managers the required liquidity. If necessary, cash flow needs will be coordinated through the System's rebalancing procedures as described in the previous section. If additional funds are required from the System's equity managers, the Director will communicate the cash flow requirements giving advanced written notice so the managers have sufficient time to comply.

Diversification

Investments shall be diversified with the intent to minimize the risk of large investment losses. Consequently, the total portfolio will be constructed and maintained to provide prudent diversification with regard to the concentration of holdings in individual issues, issuers, or industries.

Specifically, no single investment shall exceed the guidelines established under the Manager and Securities Guidelines section.

As a general rule, System assets placed with an investment manager will not represent more than 10% of that manager's assets.

Supervision

The Investment Manager shall continually supervise the investment securities in the Fund, and shall purchase, sell, substitute, redeem, or convert securities as they should deem advisable.

Brokerage Policy

All transactions effected for the System will be "subject to the best price and execution." The lowest commission rate need not mean the best realized price. Execution capability, price and overall effectiveness shall be considered, along with commission rate.

Any manager who is engaged in or has a direct pecuniary interest in a business other than investment counseling, such as a broker or dealer in securities shall not be permitted to use such business with regard to the System assets without prior written approval by the Board.

If a manager utilizes brokerage from the plan assets to effect "soft dollar" transactions, detailed records will be kept and communicated to the Board.

The Plan's investment managers shall follow the direction of the Board. It is the policy of the Board to instruct the investment managers to direct transaction orders to particular broker-dealers, including equity, fixed income, both domestic and international. The instructions from the Board currently is for the investment managers to direct as much as possible of the Plan's commission business as is practicable, subject to the best price and execution. The instruction and direction is to be construed within the normal activity of the investment manager, with no increased or decreased trading activity to occur because of the instruction. Where given discretion to establish and execute transactions through accounts with one or more broker-dealer firms as it may select, the manager must attempt to obtain "best available price and most favorable execution" with respect to all of the portfolio transactions.

Soft Dollars accumulated through the System's brokerage program may be used to pay for any System expense permitted under the regulations of the Department of Labor (including, but not limited to, legal, accounting, education, management, etc.) and approved by the Board.

Performance Objectives

Investment performance will be measured quarterly but it is not expected that the performance goals identified below will be satisfied in any single quarter or year. It is expected that these goals will be satisfied over a rolling five-year period or a full market cycle. However, action by the Board with regard to retention or dismissal of investment managers is not precluded by virtue of these time periods.

Total Fund Investments

The total fund's performance, in aggregate, will be expected to achieve a rate of return which exceeds a fund benchmark representative of the Asset Allocation objective as follows:

Benchmark	*With Private Markets*	*Without Private Markets*
Russell 1000	28%	34%
Russell 2000	7%	9%
MSCI EA FE and/or ACWI-ex US	15%	15%
Lehman Aggregate Bond Index	34%	29%
Citibank World Govt. Bond Index	7%	7%
NCREIF Property Index	6%	6%
Private Markets (S&P 500 plus 300 basis points)	3%	0%

(Procedure 610.2)

Specific guidelines and benchmarks are established below for each category of managers. Generally, however, investment managers are expected to rank in the top half of a database of similarly styled managers, and earn an average return which exceeds an appropriate index over annualized three and five year periods net of fees.

Statement of Investment Policy *Continued*

Managers are considered to have achieved this objective if their performance meets all guidelines on a cumulative three and five year annualized period. If the performance is longer than five years, the manager is expected to satisfy the performance objectives in a majority of the rolling five year periods.

Investment managers with less than five years of experience with the Fund are considered to have achieved performance objectives if their performance meets guidelines for the three year annualized time period or since inception period if the manager's track record is less than three years.

Fixed-Income Investments

The objectives for investment managers of the domestic fixed-income component of the total portfolio are:

(1) Earn an average annual return from income and capital appreciation which exceeds the Lehman Aggregate Bond Index over a three and five year annualized time period net of fees. If the performance history extends beyond five years, the manager will be required to exceed the index over a majority of the rolling five year periods.

(2) Achieve performance results which will rank in the top half of investment managers which utilize a similar investment style.

Domestic Equity Investments

The objectives for investment managers of the domestic equity component of the total portfolio are:

(1) Achieve returns which exceed an appropriate index, (i.e. S&P 500, Russell 2000, etc.) over a three and five year annualized time period net of fees. If the performance history extends beyond five years, the manager will be required to exceed the index over a majority of the rolling five year periods.

(2) Achieve performance results which will rank in the top half of investment managers which utilize a similar investment style.

Passive Equity Investment

The objective for investment managers of the passive domestic equity component of the total portfolio is to achieve returns equal to the appropriate index with minimal tracking error.

International Equity Investments

The objectives for investment managers of the international equity component of the total portfolio are:

(1) Achieve returns which exceed an appropriate index (the Morgan Stanley All Country World Ex US Index, MSCI EAFE Index) over a three and five year annualized time period net of fees. If the performance history extends beyond five years, the manager will be required to exceed the index over a majority of the rolling five year periods.

(2) Achieve performance results in the top half of investment managers which utilize a similar style of investment.

Global Fixed-Income Investments

The objective for the investment managers of the global fixed-income component of the total portfolio are:

(1) Achieve rates of return which exceed the Citibank World Government Non-Dollar Bond Index over a three and five year annualized time period net of fees. If the performance history extends beyond five years, the manager will be required to exceed the index over a majority of the rolling five year periods.

(2) Achieve returns that will rank in the top half of investment managers which utilize a similar investment style.

Real Estate Investments

(1) Achieve returns which exceed an appropriate index, (i.e. NCRIEF) net of fees over a market cycle

(2) The real estate manager(s) will be expected to achieve returns that rank in the upper half of a broad universe of real estate funds.

Private Market Investment

The Private Markets portfolio is an illiquid investment with a 10-12 year investment horizon. It is expected to provide a S&P 500 Index return plus 300 basis points over time.

Monitoring of Money Managers

(Procedure 610.4)

It is the Board's policy to monitor the portfolios of the investment managers for prudent adherence to the approved performance guidelines. Quarterly performance will be evaluated to test progress toward the attainment of longer term targets. It is understood that there are likely to be short term periods during which performance deviates from market indices. During such times, greater emphasis shall be placed on peer-performance comparisons with managers employing similar styles. In addition, manager holdings will be periodically monitored to ensure that they are adhering to expected investment styles and disciplines.

On a timely basis, but not less than four times a year, the Board will meet to focus on:

- Manager's adherence to the IPS guidelines;
- Material changes in the manager's organization, investment philosophy and/or personnel; and,
- Comparisons of the manager's results to appropriate indices and peer groups as described in the performance objectives and control section.

Statement of Investment Policy *Continued*

The risk associated with the manager's portfolio, as measured by the variability of quarterly returns (standard deviation), must not exceed that of the benchmark index and the peer group without a corresponding increase in performance above the benchmark and peer group.

Major organizational changes also warrant immediate review of the manager, including:

- Change in key professionals
- Significant account losses
- Significant growth of new business
- Change in ownership

The performance of the System's investment managers will be monitored on an ongoing basis and it is at the Board's discretion to take corrective action by replacing a manager if they deem it appropriate at any time.

Periodic Reviews of Manager Performance

The performance of each manager will be reviewed versus its benchmark every quarter. These benchmarks consist of both asset class indexes and peer group universes. Each manager's performance should exceed their passive index benchmark and each active manager should be above the median of an appropriate universe.

As good managers will occasionally have poor performance for several periods, there is some grace period permitted for performance to improve. Conversely, the performance will be reviewed with sufficient frequency to permit identification of substandard performance as quickly as possible.

Procedure:

1. Each manager is expected to produce performance equal to or better than their benchmark for three year and five year cumulative periods net of fees.
2. The expectation to produce above median performance in an appropriate peer group for three year and five year cumulative periods will be emphasized only when the majority of investment managers within the peer group are underperforming the benchmark.
3. If a manager has less than five years performance, we will review the periods reported by the consultant, such as one quarter, one year and since inception. However, no action will be taken for placement on the watch list until two years after inception date as long as the firm has not had significant organizational, personnel, or investment philosophy change.
4. If there is a failure to meet the performance objective, the following rules should be applied:

    a) A manager's (with at least two years of performance since inception) failure to meet their objective for four successive quarters will place the manager on the watch list. If a manager is consistently on the borderline, sometimes meeting objectives and sometimes failing to meet objectives, the manager may be placed on the watch list.

    b) During the next four quarters, the manager's performance will be closely monitored to see if it is warranted for the manager to be placed on probation.

    c) A manager placement on probation will result in review by the Investment Committee. When a manager is placed on probation, the Director will caution the manager against making changes from their proscribed styles or risk profile. Upon a critical review of the manager, the Investment Committee may grant up to one year further for improvement to take place upon officially recognizing the substandard performance and explicitly granting an extension of time for improvement. If there has been improvement in performance, the Investment Committee may extend the probation beyond one year.

    During the period of any such extraordinary extension, the investment staff will monitor the portfolio and transactions of such manager to ensure that excessive risk is not being taken in an attempt to "catch up". If in the judgment of the Director, such manager is managing the portfolio in such a manner that indicates that excessive risk is being taken, the Director should use the previously delegated authority to terminate or restrict the manager's activities.

5. In order to be taken off probation and placed on the watch list, a manager must beat their benchmark for 2 successive quarters net of fees (i.e. March and June) OR beat their benchmark at one-year following four quarters of good performance.
6. In order to be taken off the watch list, a manager must beat their benchmark for an additional 2 successive quarters net of fees (i.e. September and December) OR have an additional four quarters of good performance.
7. Extraordinary events (described below) that are deemed likely to negatively impact the manager's organization or investment process may also result in a manager being placed on watch list or probation, regardless of the manager's performance.

Extraordinary Reviews of Managers

If an event occurs within a manager's organization or is likely to impact the manager's organization, the Director, Retirement Services, shall make a determination whether such event compromises the investment process or in any other manner might negatively impact the management of the Plan's assets.

Statement of Investment Policy *Continued*

Such events would include but are not limited to:

a) Loss of any significant investment professional directly involved with the management of Plan assets or of such significance to the manager's overall investment process as to call into question the future efficacy of that process.

b) Sale, offers for sale, or offer to purchase the manager's business to/by another entity.

c) Significant financial difficulty or loss of a sizable portion of the manager's assets under management.

d) Filing or announcement of regulatory action of non-trivial nature, particularly that involving violations of the Investment Advisers Act of 1940, the Securities Act of 1933, or the Securities Exchange Act of 1934, or any state Blue Sky Law to which the manager is subject.

e) Any other event which in the discretion of the Director appear to put the Fund's assets at risk of loss, either actual or opportunity. Examples of such events include performance and/or risk that is inconsistent with the manager's stated investment approach and a flagrant violation of guidelines.

Any of these events may trigger a due diligence visit to the firm by the Investment Committee, being placed on the watch list, being put on probation or termination depending on the seriousness of the event and the probability of impacting the management of the Plan's assets.

Exceptions

The Board may grant specific exceptions to any part of the Investment Policy Statement where in their judgment the exception may add value to the fund without undue risk.

Investment Professionals

INVESTMENT MANAGERS

Domestic Equities

Atlanta Capital Management
Large Cap Growth
Atlanta, GA

Brandywine Asset Management
Small Cap Value
Philadelphia, PA

Eagle Asset Management, Inc.
Small Cap Growth
St. Petersburg, FL

Northern Trust Global Investments
Russell 3000 Index
Chicago, IL

Domestic Equities *Continued*

Dodge & Cox
Large Cap Value
San Francisco, CA

Wellington Management
All Cap Growth
San Francisco, CA

Private Equities

Pantheon Ventures, Inc.
Private Market Equities
San Francisco, CA

Pathway Capital Management, LLC
Private Market Equities
Irvine, CA

International Equities

The Boston Company Asset Management, LLC
Boston, MA

Fisher Investments Institutional Group
Woodside, CA

McKinley Capital Management
Anchorage, AK

Domestic Fixed Income

Dodge & Cox
San Francisco, CA

BlackRock Financial Management
New York, NY

Global Fixed Income

Loomis Sayles
Boston, MA

Real Estate

American Realty Advisors
Glendale, CA

DRA Advisors, Inc.
New York, NY

Fidelity Investments
Boston, MA

GE Asset Management
Stamford, CT

MIG Realty Advisors
Cleveland, OH

Prudential Real Estate Investors
Newark, NJ

CONSULTANTS

The Northern Trust
Chicago, IL

Strategic Investment Solutions, Inc.
San Francisco, CA

CUSTODIAN

The Northern Trust
Chicago, IL

PROXY VOTING

Glass Lewis & Co. LLC
San Francisco, CA

Schedule of Investment Results

GROSS PERFORMANCE SUMMARY BY ASSET CLASS

For Periods Ending June 30, 2007

	One Year	*Three Years*	*Five Years*
Total Fund	**16.2%**	**11.7%**	**11.8%**
Benchmark	15.7%	11.5%	10.8%
TUCS All Master Trust Median	16.4%	11.6%	10.8%
TUCS Public Fund Universe Median	16.1%	11.8%	10.9%
Total Domestic Equity	**20.0%**	**12.7%**	**11.6%**
S&P 500 Index	20.6%	11.7%	10.7%
TUCS Equity Median	19.8%	13.6%	12.9%
Total International Equity	**27.2%**	**22.8%**	**17.2%**
MSCI ACWI ex-US (Net Div.)	29.6%	24.5%	19.5%
TUCS International Equity Median	28.3%	23.3%	19.0%
Total Domestic Fixed Income	**6.1%**	**4.5%**	**5.2%**
Lehman Brothers Aggregate Bond Index	6.1%	4.0%	4.5%
TUCS Domestic Fixed Income Median	6.1%	4.3%	4.9%

	One Quarter	*One Year*
Total Global Fixed Income	**-0.9%**	**4.6%**
Citigroup World Government Bond Index	-1.5%	2.9%
TUCS Unhedged Global Fixed Income Median	-0.6%	5.4%

	One Year	*Three Years*	*Five Years*
Total Real Estate	**21.7%**	**18.4%**	**18.9%**
NCREIF Property Index	17.2%	18.0%	14.4%
TUCS Real Estate Median	15.2%	19.3%	15.5%

Basis of Calculation: Time-Weighted Rate of Return

Source: The Northern Trust Investment Performance Evaluation Report June 30, 2007

Schedule of Investment Results *Continued*

NET PERFORMANCE SUMMARY BY INVESTMENT MANAGER

For Periods Ending June 30, 2007

The table below details the rates of return for the System's investment managers over various time periods.
Returns for one year or greater are annualized. Each "+" represents a benchmark the manager has outperformed.

	One Year	*Three Years*	*Five Years*
Domestic Fixed Income			
Northern Trust (Index)	20.2%++	12.5%+	11.5%=
Russell 3000 Index	20.1%	12.4%	11.5%
TUCS Equity Median	19.8%	13.6%	12.9%
Atlanta Capital (Large Cap Growth)	17.1%+	8.9%+	7.4%
Russell 1000 Growth Index	19.1%	8.7%	9.3%
TUCS Large Cap Growth Median	16.4%	9.9%	9.7%
TUCS Equity Median	19.8%	13.6%	12.9%
Eagle Asset Management (Small Cap Growth)	29.5%+++	17.4%+++	16.1%+++
Russell 2000 Growth Index	16.8%	11.8%	13.1%
TUCS Small Cap Growth Median	17.8%	13.7%	15.1%
TUCS Equity Median	19.8%	13.6%	12.9%
Brandywine (Small Cap Value)	17.4%+	13.2%	13.7%+
Russell 2000 Value Index	16.1%	15.0%	14.6%
TUCS Small Cap Value Universe Median	18.2%	15.4%	16.3%
TUCS Equity Median	19.8%	13.6%	12.9%

	One Quarter	*One Year*	*Three Years*
Dodge & Cox (Large Cap Value)	5.5%+	19.2%	15.7%++
Russell 1000 Value Index	4.9%	21.9%	15.9%
TUCS Large Cap Value Median	6.4%	22.3%	15.6%
TUCS Equity Median	6.2%	19.8%	13.6%

	One Quarter	*One Year*	*Inception (09/05)*
Wellington Management	8.3%+++	16.9%	11.5%
Russell 3000 Growth Index	6.8%	18.8%	11.7%
TUCS All Cap Growth Median	6.9%	17.6%	N/A
TUCS Equity Median	6.2%	19.8%	N/A

	One Quarter	*One Year*	*Three Years*
International Equity			
Boston Company Asset Management, LLC	7.4%=	23.0%	19.8%
MSCI ACWI ex-US Index	8.2%	29.6%	24.5%
TUCS International Equity Median	7.4%	28.3%	23.3%

	One Quarter	*One Year*	*Inception (07/05)*
Fisher Investments Institutional Group	9.6%++	25.6%	26.4%
MSCI ACWI ex-US Index	8.2%	29.6%	28.8%
TUCS International Equity Median	7.4%	28.3%	N/A
McKinley Capital Management	8.3%++	30.9%++	32.6%+
MSCI ACWI ex-US Index	8.2%	29.6%	28.8%
TUCS International Equity Median	7.4%	28.3%	N/A

Basis of Calculation: Time-Weighted Rate of Return

Source: The Northern Trust Investment Performance Evaluation Report June 30, 2007

SCHEDULE OF INVESTMENT RESULTS *Continued*

NET PERFORMANCE SUMMARY BY INVESTMENT MANAGER *Continued*

For Periods Ending June 30, 2007

	One Quarter	*One Year*	*Three Years*
Domestic Fixed Income			
BlackRock Financial Management, Inc.	-0.9%	5.0%	3.9%
Lehman Brothers Aggregate Bond Index	-0.5%	6.1%	4.0%
TUCS Fixed Income Median	-0.3%	6.1%	4.3%

	One Year	*Three Years*	*Five Years*
Dodge and Cox	6.9%++	4.5%++	5.3%++
Lehman Brothers Aggregate Bond Index	6.1%	4.0%	4.5%
TUCS Fixed Income Median	6.1%	4.3%	4.9%

	One Quarter	*One Year*	*Inception (02/05)*
Global Fixed Income			
Loomis Sayles	-1.0%+	4.2%+	1.4%+
Citigroup World Government Bond Index	-1.5%	2.9%	-0.1%
TUCS International Fixed Portfolio Median	-0.6%	5.4%	N/A

	One Year	*Three Years*	*Five Years*
Real Estate			
MIG Realty Advisors	7.27%	8.49%	8.65%
DRA II	105.3%++	39.3%++	25.9%++
Fidelity	75.6%++	46.8%++	32.2%++
NCREIF Property Index	17.2%	18.0%	14.4%
TUCS Real Estate Median	15.2%	19.3%	15.5%

	One Quarter	*One Year*	*Inception (06/04)*
Prudential (PRISA)	5.9%++	17.5%++	18.7%+
NCREIF Property Index	4.6%	17.2%	18.0%
TUCS Real Estate Median	3.1%	15.2%	N/A

	One Quarter	*One Year*	*Inception (09/05)*
DRA V	1.4%	9.0%	6.5%
NCREIF Property Index*	3.6%	16.6%	20.2%
TUCS Real Estate Median	3.1%	15.2%	N/A

**Quarter Lag*

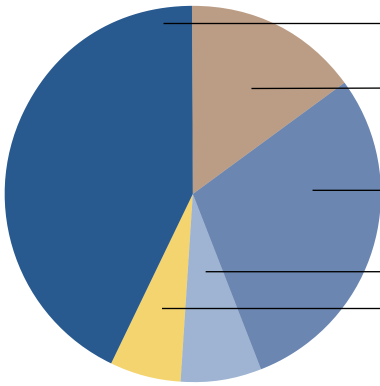
Basis of Calculation: Time-Weighted Rate of Return

Source: The Northern Trust Investment Performance Evaluation Report June 30, 2007

Investment Review

TARGET ASSET ALLOCATION

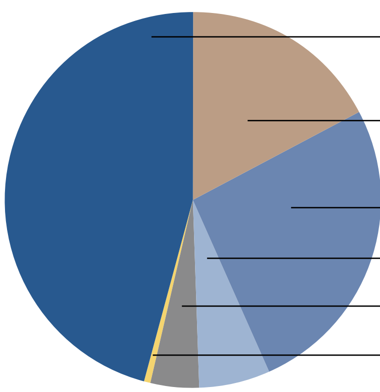
As of June 30, 2007



Domestic Equity	43%
International Equity	15%
Domestic Fixed Income	29%
Global Fixed Income	7%
Real Estate	6%

ACTUAL ASSET ALLOCATION

As of June 30, 2007 (Dollars in Millions)



Domestic Equity	45.8%	$852.85
International Equity	17.3%	$322.55
Domestic Fixed Income	26.1%	$485.35
Global Fixed Income	6.0%	$112.10
Real Estate	4.4%	$81.37
Cash	0.4%	$6.42

ACTUAL ASSET ALLOCATION

As of June 30, 2007
(Dollars in Millions)

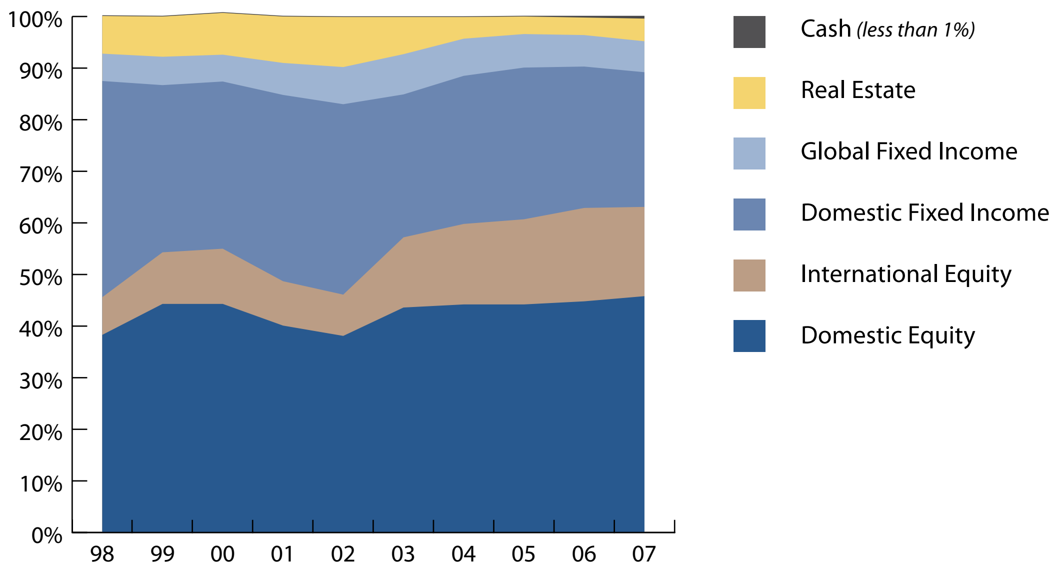
Asset Class	*Actual*
Domestic Equity	$ 852.85
International Equity	322.55
Domestic Fixed Income	485.35
Global Fixed Income	112.10
Real Estate	81.37
Cash	6.42
TOTAL	**$1,860.64**

Non-GAAP Basis

Investment Review *Continued*

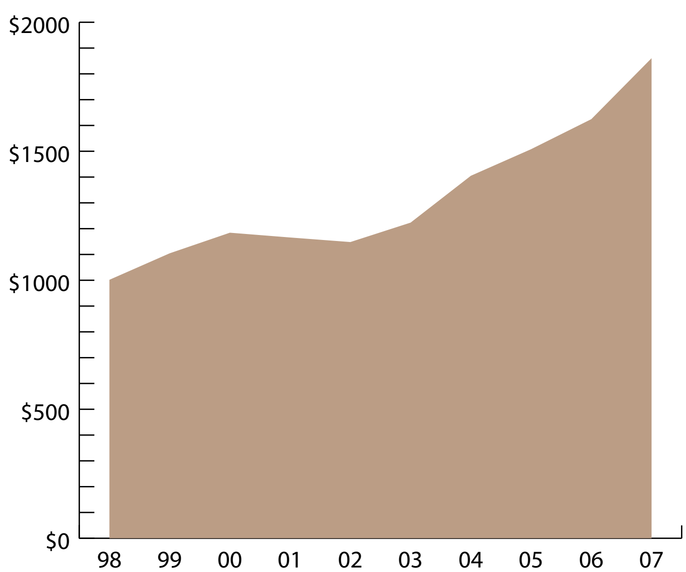
HISTORICAL ASSET ALLOCATION (ACTUAL)

June 30, 1998 – June 30, 2007



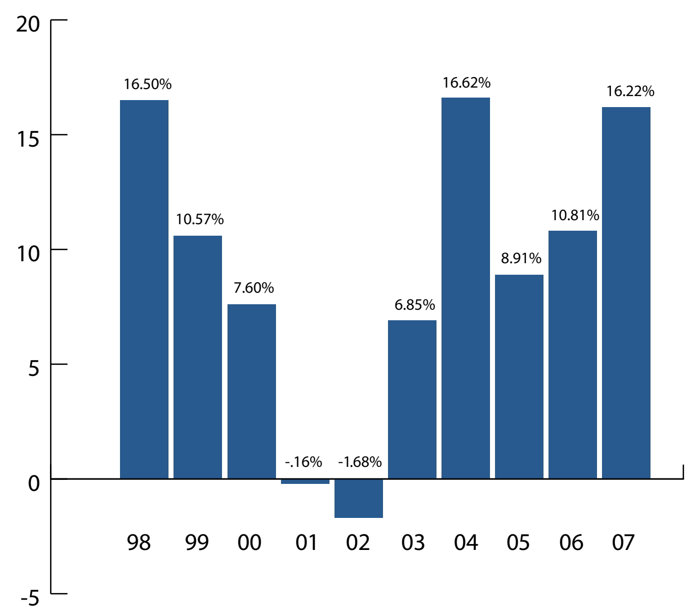
MARKET VALUE GROWTH OF PLAN ASSSETS

For Ten Years Ended June 30, 2007 (Dollars in Millions)



HISTORY OF PERFORMANCE FOR FISCAL YEARS 1998–2007

(Based on Market Value)



List of Largest Assets Held

LARGEST STOCK HOLDINGS *(By Market Value)*
June 30, 2007

Shares	Country	Description	Market Value in $US
220,900	United States	CISCO SYS INC COM	$6,152,065.00
145,060	United States	GENERAL ELEC CO COM	5,552,896.80
190,360	United States	COMCAST CORP NEW CL A CL A	5,352,923.20
58,630	France	GROUPE DANONE EUR0.25 (POST SUBDIVISION)	4,752,548.32
218,560	United States	ORACLE CORP COM	4,307,817.60
80,240	United States	MERCK & CO INC COM	3,995,952.00
47,000	United States	BAKER HUGHES INC COM	3,954,110.00
26,350	Germany	SIEMENS AG NPV(REGD)	3,792,505.69
159,430	United States	STAPLES INC COM	3,783,273.90
71,420	United States	MEDTRONIC INC COM	3,703,841.20

LARGEST BOND HOLDINGS *(By Market Value)*
June 30, 2007

Description	Country	Maturity Date	Par Value	Market Value in $US
FNMA 30 YEARS SINGLE FAMILY MTG 6 30 YEARS SETTLES JUL	United States	7/15/34	22,200,000.00	$21,957,176.40
FNMA 30 YEAR PASS-THROUGHS 5.5% 30 YEARSSETTLES JULY	United States	7/15/34	19,500,000.00	18,805,312.50
UNITED STATES TREAS NTS DTD 00013 3% DUE11-15-2007 BEO	United States	11/15/07	11,000,000.00	10,922,659.00
FNMA POOL #844809 5% 11-01-2035 BEO	United States	11/1/35	11,309,555.76	10,625,836.57
UNITED STATES TREAS NTS DTD 02/18/2003 3% DUE 02-15-2008 REG	United States	2/15/08	9,000,000.00	8,888,202.00
FHLMC 30 YEAR GOLD PARTICIPATION CTF (PC) 5.5 30 YEARS SETTLES AUG	United States	8/14/07	9,000,000.00	8,676,558.00
FHLMC POOL #1H-2623 5.81 07-01-2036	United States	7/1/36	6,863,950.21	6,830,447.26
US TREAS NTS DTD 11/16/1998 4.75 DUE 1-15-2008 REG	United States	11/15/08	6,500,000.00	6,479,180.50
FNMA POOL #735503 6% 04-01-2035 BEO	United States	4/1/35	6,341,342.66	6,304,163.36
JAPAN (GOVT OF) 0.2% BDS 20/09/07 JPY'236'	Japan	9/20/07	717,000,000.00	5,802,071.18

Schedule of Investment Fees

	*Assets Under Management at Market Value**	*Fees*	*Basis Points*
Investment Managers' Fees			
Domestic Equity	$824,698,000	$1,911,549	23
Private Market	28,151,000	741,982	264
International Equity	322,547,000	1,772,220	55
Domestic Fixed Income	485,352,000	919,340	19
Global Fixed Income	112,101,000	372,912	33
Real Estate	81,366,000	993,413	122
Cash	6,427,000	-	N/A
TOTAL	**$1,860,642,000**	**$6,711,416**	**36**

Other Investment Service Fees			
Investment Consultant	N/A	$120,000	N/A
Proxy Voting	N/A	3,900	N/A
Custodian	N/A	5,855	N/A
Real Estate Legal Fees	N/A	449	N/A
Real Estate Appraisals	N/A	-	N/A
TOTAL		**$130,204**	

** Includes Cash in Managers' Accounts; Non-GAAP Basis*

Schedule of Commissions

Brokerage Firm	Number of Shares Traded	Total Commissions	Commission Per Share
ABEL NOSER CORPORATION	5,600	$ 224.00	$0.04000
ADAMS HARKNESS & HILL, INC	5,240	209.60	0.04000
ADP CLEARING & OUTSOURCING INC	80,660	1,814.91	0.02250
ARNHOLD & S BLEICHROEDER INC	32,435	1,070.60	0.03301
ASSENT	451,585	3,161.13	0.00700
AVONDALE PARTNERS	245	8.00	0.03265
B TRADE SERVICES	236,712	5,774.75	0.02440
BANC AMERICA SECUR MONTGOMERY DIV	506,436	18,776.96	0.03708
BAYPOINT TRADING LLC	14,870	383.00	0.02576
BEAR STEARNS 57079	352,675	14,103.50	0.03999
BERNSTEIN, SANFORD C & CO	121,870	2,756.30	0.02262
BLAIR, WILLIAM & CO	26,215	1,048.60	0.04000
BNY ESI SECURITIES CO	326,930	2,540.70	0.00777
BOENNING & SCATTERGOOD NFS	51,110	1,149.84	0.02250
BOENNING AND SCATTERGOOD	51,680	1,153.89	0.02233
BROADCORT CAPITAL CORP	24,170	966.80	0.04000
BROWN BROTHERS, HARRIMAN & CO NEW YORK	6,300	283.50	0.04500
CANTOR FITZGERALD & CO	96,625	2,709.45	0.02804
CAP INSTITUTIONAL SERVICES INC	194,600	7,858.00	0.04038
CIBC WORLD MARKETS CORP NEW YORK	80,115	2,816.20	0.03515
CITATION GROUP	8,000	360.00	0.04500
CITIGROUP GLOBAL MARKETS INC/SMITH BARNEY	396,565	13,630.25	0.03437
COLLINS STEWART INC	2,030	81.20	0.04000
COWEN LLC	19,670	779.10	0.03961
CRAIG HALLUM	5,980	239.20	0.04000
CREDIT RESEARCH & TRADING CORP	13,620	544.80	0.04000
CREDIT SUISSE FIRST BOSTON CORPORATION	282,107	9,567.67	0.03392
CROWELL WEEDON AND CO	5,260	210.40	0.04000
CRUTTENDEN AND COMPANY	12,480	393.85	0.03156
DAHLMAN ROSE & COMPANY	6,290	251.60	0.04000
DAVENPORT AND CO OF VIRGINIA INC	6,475	323.75	0.05000
DAVIS MENDEL AND REGENSTEIN INC	2,000	90.00	0.04500
DEUTSCHE BANK SECURITIES INC	203,030	7,519.11	0.03703
DONALDSON & CO INCORPORATED	4,400	198.00	0.04500
E TRADE CLEARING LLC	670	26.80	0.04000
EDWARDS A G	45,040	1,976.60	0.04389

Schedule of Commissions *Continued*

Brokerage Firm	Number of Shares Traded	Total Commissions	Commission Per Share
EMP RESEARCH PTRNS LLC	10,800	$ 432.00	$0.04000
FIDELITY CAPITAL MARKETS	2,630	59.18	0.02250
FIRST ALBANY CORPORATION	35,040	1,315.60	0.03755
FOX PITT KELTON	15,585	623.40	0.04000
FRIEDMAN BILLING AND RAMSEY	59,905	2,335.50	0.03899
GFI SECURITIES LLC	195	3.90	0.02000
GOLDMAN EXECUTING & CLEARING	588,298	3,041.02	0.00517
GOLDMAN SACHS & COMPANY	184,773	7,304.29	0.03953
HARRIS NESBITT CORP	10,545	421.80	0.04000
HEFLIN & CO, LLC	26,110	1,044.40	0.04000
HIBERNIA SOUTHCOAST CAPITAL INC	8,660	346.40	0.04000
HSBC BROKERAGE USA	8,520	355.20	0.04169
ING FINANCIAL MARKETS LLC	9,600	288.00	0.03000
INSTINET	58,090	1,558.12	0.02682
INVESTMENT TECHNOLOGY GROUP INC	1,539,287	20,558.63	0.01336
IPS BROKERAGE INC	313,246	14,096.07	0.04500
ISI GROUP INC	23,200	1,071.00	0.04616
J P MORGAN SECURITIES INC	89,315	3,208.85	0.03593
JAMES CAPEL SECURITIES, INC	7,850	312.48	0.03981
JEFFERIES & COMPANY	164,035	5,361.18	0.03268
JMP SECURITIES	26,500	795.00	0.03000
JNK SECURITIES INC	1,935	38.70	0.02000
JOHNSON RICE & CO	4,160	163.00	0.03918
JONES & ASSOCIATES	103,575	3,321.00	0.03206
JONES AD	25,965	1,038.60	0.04000
JONESTRADING INST SERV	67,230	2,016.90	0.03000
KALB VOORHIS & CO	3,660	82.36	0.02250
KAUFMAN BROTHERS	9,700	388.00	0.04000
KEEFE BRUYETTE AND WOODS INC	8,235	329.40	0.04000
KELLOGG PARTNERS	9,580	215.55	0.02250
KINNARD JOHN G & COMPANY	1,740	69.60	0.04000
KNIGHT SECURITIES L P	161,977	5,971.93	0.03687
LA BRANCHE FINANCIAL #2	9,630	218.19	0.02266
LAZARD FRERES & CO	4,090	182.60	0.04465
LEERINK SWANN & CO /IPO	54,090	1,895.15	0.03504
LEHMAN BROTHERS INC	183,980	6,255.60	0.03400
LEHMAN BROTHERS INC NEW YORK	404,886	9,412.08	0.02325

Schedule of Commissions *Continued*

Brokerage Firm	Number of Shares Traded	Total Commissions	Commission Per Share
LIQUIDNET INC	465,570	$ 11,970.15	$0.02571
LOOP CAPITAL MARKETS/BROADCORT CAPITAL	3,140	125.60	0.04000
LYNCH JONES & RYAN	1,380,636	51,714.92	0.03746
MCDONALD AND COMPANY/KEYBANC	25,740	1,021.40	0.03968
MELVIN SECURITIES	1,950	58.00	0.02974
MERRILL LYNCH PIERCE FENNER & SMITH	257,802	8,454.48	0.03279
MERRILL PROFESSIONAL CLEARING CORP	75,380	1,926.50	0.02556
MERRIMAN CURHAN FORD & CO	23,660	756.40	0.03197
MIDWEST RESEARCH SECURITIES	9,070	238.55	0.02630
MILETUS TRADING LLC	22,850	478.25	0.02093
MILLER TABAK & CO LLC	16,180	647.20	0.04000
MORGAN KEEGAN AND COMPANY	10,235	442.85	0.04327
MORGAN STANLEY & CO INC NEW YORK	428,480	11,138.05	0.02599
NATIONAL FINANCIAL SERVICES	26,610	989.65	0.03719
NBC CLEARING SERVICE TWO	24,510	980.40	0.04000
NEEDHAM & COMPANY	31,780	1,303.40	0.04101
NYFIX CLG CORP	11,610	282.05	0.02429
PACIFIC AMERICAN SECURITIES LLC	4,500	135.00	0.03000
PACIFIC GROWTH EQUITIES	1,260	50.40	0.04000
PERSHING DIV/DONALDSON LUFKIN/JE	3,900	175.50	0.04500
PERSHING LLC FORMERLY DLJ	25,980	812.40	0.03127
PIPELINE TRADING SYSTEMS LLC	56,680	1,956.20	0.03451
PIPER JAFFRAY INC	146,790	5,120.20	0.03488
POLCARI WEICKER DIV OF GARBAN	1,300	29.25	0.02250
PRITCHARD CAPITAL PARTNERS LLC	15,060	602.40	0.04000
PRUDENTIAL EQUITY GROUP	83,533	3,203.89	0.03835
PULSE TRADING LLC	82,010	1,848.25	0.02254
RAYMOND JAMES	13,980	586.20	0.04193
RBC CAPITAL MARKETS INC	45,640	1,231.28	0.02698
ROBBINS AND HENDERSON	25,760	579.61	0.02250
ROBERT W BAIRD & COMPANY INC MILWAUKEE USA	47,300	1,896.65	0.04010
SANDLER O'NEILL & PARTNER	2,700	121.50	0.04500
SCOTIA MCLEOD INC	7,960	318.40	0.04000
SCOTT & STRINGFELLOW INVESTMENT	700	28.00	0.04000
SG COWEN AND COMPANY	3,300	99.00	0.03000
SG COWEN SECURITIES	57,000	2,186.40	0.03836
SIMMONS & COMPANY INTL	990	39.60	0.04000

Schedule of Commissions *Continued*

Brokerage Firm	Number of Shares Traded	Total Commissions	Commission Per Share
SOCIETE GENERALE SECURITIES CORPO	200	$ 6.00	$0.03000
SOLEIL SECURITIES CORP	1,700	76.50	0.04500
STANDFORD GROUP CO	21,580	863.20	0.04000
STATE STREET BROKERAGE SVCS	8,710	261.30	0.03000
STEPHENS INC	4,300	172.00	0.04000
STERNE AGEE AND LEACH INC	10,355	414.20	0.04000
STIFEL NICOLAUS AND COMPAN	127,660	3,622.70	0.02838
SUNTRUST ROBINSON HUMPHREY	45,990	1,844.10	0.04010
THOMAS WEISEL PARTNERS 226	154,205	6,082.30	0.03944
TRINITY TRADING CORPORATION	1,625	32.50	0.02000
UBS WARBURG LLC	157,510	5,795.15	0.03679
UBS/WARBURG SECURITIES LLC NEW YORK	229,130	8,918.40	0.03892
UNTERBERG HARRIS	3,220	128.80	0.04000
VERITAS SECURITIES	45,300	1,359.00	0.03000
WACHOVIA CAPITAL MARKETS 46171	21,120	834.80	0.03953
WACHOVIA CAPITAL MARKETS LLC	18,560	742.40	0.04000
WEDBUSH MORGAN SECURITIES, INC	11,755	510.45	0.04342
WEEDEN AND & CO	63,705	2,228.90	0.03499
WHITE CAP TRADING LLC	1,700	54.00	0.03176
WR HAMBRECHT & CO	14,035	561.40	0.04000
TOTAL	**12,300,213**	**$349,188.82**	**$0.02839**

Investment Summary

As of June 30, 2007
(Dollars in thousands)

Type of Investment	*Market Value*	*% of Portfolio*
EQUITIES		
Consumer Discretionary	$ 52,692	2.83%
Consumer Staples	12,752	0.69%
Energy	23,528	1.26%
Financials	54,054	2.91%
Health Care	39,831	2.14%
Industrials	48,689	2.62%
Materials	17,685	0.95%
Technology/Telecommunication	110,495	5.94%
Utilities	8,383	0.45%
Miscellaneous	3,834	0.21%
Commingled	412,624	22.18%
Foreign Equities	347,753	18.69%
TOTAL EQUITIES	**$1,132,320**	**60.87%**
FIXED INCOME		
U.S. Treasury	$ 40,787	2.19%
U.S. Government Agency	251,560	13.52%
Domestic Corporate Bonds	210,270	11.30%
Foreign Government	62,938	3.38%
Foreign Corporate	38,884	2.09%
TOTAL FIXED INCOME	**$ 604,439**	**32.48%**
OTHER INVESTMENTS		
Short Term	$79,460	4.26%
Real Estate	81,332	4.37%
Private Market Equities	26,956	1.45%
TOTAL OTHER INVESTMENTS	**$ 187,748**	**10.08%**
PENDINGS	**$ (63,864)**	**(3.43)%**
TOTAL	**$1,860,643**	**100.00%**

Investment Property

MILPITAS WAREHOUSE

145,152 square-foot warehouse/distribution building, equally divided into four bays. Acquired jointly with the Police & Fire Department Retirement Plan in February 1986. The System purchased the Police & Fire Department Retirement Plan's 50% interest in the property in November 2003.

Actuarial Section

Actuary Certification Letter

GRS Gabriel Roeder Smith & Company
Consultants & Actuaries

Gabriel Roeder Smith & Company
Consultants & Actuaries
9171 Towne Centre Drive, Suite 440
San Diego, CA 92122-1238

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www.gabrielroeder.com

August 29, 2006

Board of Administration
City of San José
Federated City Employees' Retirement System
1737 North First Street, Suite 580
San José, CA 95112-4505

RE: ACTUARIAL VALUATION CERTIFICATION

Dear Members of the Board:

The actuarial valuation report for the City of San Jose Federated City Employees' Retirement System, completed as of June 30, 2005, reveals that the assets of the Federated Retirement System along with future contributions at the level recommended in that report are expected to fully support the benefits of the System. This conclusion is based on financial and demographic data as of the valuation date and on current actuarial assumptions, which are based on the System's demographic and economic experience. This letter serves as the Actuary's certification letter and offers our independent actuarial review opinion.

In support of this opinion and certification, we have included the following information:

- The funding objective of the plan.
- The frequency of the plan's actuarial valuations and date of the most recent actuarial valuation.
- The source and degree of verification of the data used in the actuarial valuation.
- Supporting schedules that we have prepared and attached.
- The extent of our responsibility for the trend data schedules in the financial section of the report.
- The assumptions and methods used to value plan assets and liabilities relative to the Government Accounting Standards Board (GASB) Statement No. 25.
- Other disclosure information.

The Funding Objective of the Plan

Chapters 3.28 and 3.44 of the San Jose Municipal Code and related ordinances establish that the required annual contribution to the plan, shared by the City and members is such that contribution rates, over time, shall remain level as a percentage of payroll.

Actuary Certification Letter *Continued*

GRS Gabriel Roeder Smith & Company
Consultants & Actuaries

This funding objective is currently being realized through contributions sufficient to pay the System's normal cost as well as amortizing unfunded liabilities over a combination of 30 years and the present value of future salaries.

The Frequency of the Plan's Actuarial Valuations and Date of the most Recent Actuarial Valuation

This plan is valued on a bi-annual basis, as of June 30. The most recent actuarial valuation was completed as of June 30, 2005.

The Source and Degree of Verification of the Data Used in the Actuarial Valuation

Computer files containing data on System membership as of June 30, 2005 were provided by the City of San Jose Department of Retirement Services. While these files were not audited, the data was checked for internal consistency and was reviewed for reasonableness and consistency in relation to the data provided for the prior valuation.

Asset-related data were also received from the City of San Jose Department of Retirement Services and were used without further audit in the development of the actuarial value of assets.

Supporting Schedules

We have prepared the following supporting schedules for inclusion in this Financial Statement:

- Summary of actuarial assumptions and methods.
- Schedule of active member valuation data.
- Schedule of retirants and beneficiaries added to and removed from rolls.
- Solvency test.
- Analysis of financial experience.

Trend Data Schedules in the Financial Section

All of the trend data information in the financial section of the report was calculated and summarized by Gabriel, Roeder, Smith & Co.

Actuarial Assumptions and Methods Used for Funding Purposes

The assumptions and methods used for funding purposes meet the parameters set for the disclosures presented in the financial section by Government Accounting Standards Board (GASB) Statement No. 25, Financial Reporting for Defined Benefit Plans and Note Disclosures for Defined Contribution Plans. In our opinion, the assumptions are reasonably related to past experience and represent our best estimate of future conditions affecting the System. Nevertheless, the emerging costs of the System will vary from those presented in this report to the extent actual experience differs from that projected by the actuarial assumptions.

ACTUARY CERTIFICATION LETTER *Continued*

GRS Gabriel Roeder Smith & Company
Consultants & Actuaries

Each of the signatories is a Fellow of the Society of Actuaries, an Enrolled Actuary, and a Member of the American Academy of Actuaries. Combined, we have over 65 years of experience in performing valuations for public retirement systems

Sincerely,

Norman S. Losk, FSA, EA, MAAA
Senior Consultant

Rick A. Roeder, FSA, EA, MAAA
Senior Consultant

Summary of Assumptions and Funding Method

Actuarial Valuation Cost Method. The Entry Age Normal Cost Method is used for the retirement benefits of the System

Financing of Unfunded Actuarial Accrued Liability. The balance of unfunded actuarial accrued liabilities was amortized by level percent of payroll contributions over a 30-year period.

Asset Valuation Method. The Actuarial Value of Assets recognizes 20% of total return in excess of (or less than) the investment return assumption for each of the last five years. This method has the effect of smoothing volatility in investment returns.

The Investment Return Rate used for the actuarial valuation calculations was 8.25% a year, net of administrative expenses, compounded annually. This assumption is used to equate the value of payments due at different points in time. The rate is comprised of two elements:

Inflation	4.00% (4.5% in previous valuation)
Real Rate of Return	4.25% (3.75% in previous valuation)
Total	**8.25%**

Salary Increase Rates used to project current pays to those upon which a benefit will be based are represented by the following table. Rates do not vary by age, but do reflect an added merit component, for those with 0–4 years of service at the valuation date.

The rate of annual salary increase for all members with at least 5 years of service is set out in the following:

Inflation	4.00%
Merit and Longevity	0.25%
Total	**4.25%**

The rate of annual salary increase for all members with less than 5 years of service equal to the 4.25% set out above plus the appropriate value from the following table:

Years of Service at Valuation Date	Merit/Longevity
0	5.50%
1	3.50%
2	2.00%
3	1.50%
4	0.75%

Interest credited to member contributions is 3.0%, compounded annually.

Sample rates of separation from active membership are shown below (rates do not include separation on account of retirement or death). This assumption measures the probabilities of members remaining in employment.

% of Active Members Separating Within Next Year

Sample Ages	Disability[1]	Withdrawal	Vested Termination[2]
20	.04%	11.00%	-%
25	.06	7.00	3.00
30	.07	5.00	3.00
35	.09	2.50	2.75
40	.15	1.50	2.00
45	.25	1.25	2.00
50	.40	1.25	1.50
55	.50	1.00	0.00
60	1.00	1.00	0.00
65	2.00	0.00	0.00
70	0.00	0.00	0.00

[1] 50% of the disabilities are assumed to be duty-related and 50% are assumed to be non-duty related.

[2] 30% of terminating employees who leave their contributions in the Plan, with 5+ years of service, are assumed to subsequently work for a reciprocal employer and receive 4.0% pay increases per year. (Previous valuation not explicitly valued.)

For inactive members, the assumed age at retirement is age 58 (previous assumption was 60).

If an inactive member is not vested, the liability valued is their employee contributions with interest.

The post-retirement mortality table used for healthy retirees and beneficiaries was the 1994 Group Annuity Mortality Table (sex distinct). The previous valuation used the 1983 Group Annuity Mortality Table for males with a one-year setback, and for females, with a one-year set forward). The disabled mortality table used was the 1981 Disability Mortality Table. This assumption is used to measure the probabilities of members dying after retirement and the probabilities of each benefit payment being made after retirement. Related values are shown below.

	Future Life Expectancy (Years)			% of Benefit Recipients Dying Each Year		
Sample Ages	Retired Men	Retired Women	Disabled	Retired Men	Retired Women	Disabled
45	35.4	39.7	23.6	0.16%	0.10%	2.08%
50	30.7	34.9	21.1	0.26	0.14	2.44
55	26.2	30.2	18.7	0.44	0.23	2.84
60	21.8	25.6	16.4	0.80	0.44	3.30
65	17.8	21.3	14.1	1.45	0.86	3.79
70	14.3	17.3	11.7	2.37	1.37	4.37
75	11.1	13.6	9.2	3.72	2.27	5.53
80	8.4	10.3	7.0	6.20	3.94	8.74

The active member mortality assumption measures the probability of mortality before retirement. The new rates include probability of ordinary death, service death, and death while eligible for retirement or disability.

% of Active Members Dying Each Year

Sample Ages	Men	Women
30	.06%	.05%
35	.06	.05
40	.07	.06
45	.09	.08
50	.16	.13
55	.26	.20
60	.38	.30
65	.53	.44

Summary of Assumptions and Funding Method *Continued*

The rates of retirement used to measure the probability of eligible active members retiring during the next year.

% of Active Members Retiring Within the Next Year*

Retirement Ages	% of Active Members Retiring Within the Next Year	Retirement Ages	% of Active Members Retiring Within the Next Year
55	15.0%	63	10.0%
56	7.5	64	10.0
57	7.5	65	25.0
58	7.5	66	25.0
59	7.5	67	25.0
60	7.5	68	25.0
61	7.5	69	25.0
62	20.0	70	100.00

**Superceded by 50% retirement probability each year after completion of 30 years of service and attainment of age 50.*

Disability Benefit Offset. Workers' Compensation Benefits are assumed to not be an offset.

Survivor Benefits. Marital status and spouses' census data were imputed with respect to active and deferred members.

Marital Status: 75% of men (85% in the previous valuation) and 55% of women (60% in the previous valuation) were assumed married at retirement.

Spouse Census: Women were assumed to be 3 years younger than men.

"Spouse" is assumed to encompass a registered domestic partner.

Health Subsidy Benefits

Increase in Retiree Population: The covered Retiree population is assumed to increase 6.10% per year.

Covered Payroll Increase: 4.0% per year. (4.5% previous valuation)

Medical and Dental Trend Rate: 7.50%

Schedule of Active Member Valuation Data

June 30, 1995 to June 30, 2005

Valuation Date	Number	Annual Payroll	Annual Average Pay	% Increase in Average Pay
June 30, 2005	4,148	$286,445,861	$69,056	5.6%
June 30, 2003	4,479	$292,961,371	$65,408	15.6%
June 30, 2001	4,466	$252,696,000	$56,582	7.9%
June 30, 1999	3,694	$193,650,000	$52,423	8.3%
June 30, 1997	3,642	$176,284,000	$48,403	6.8%
June 30, 1995	3,397	$153,918,000	$45,310	4.4%

Changes in Retirants *(Including Beneficiaries)*

July 1, 1995 to June 30, 2005

	Beginning of Period		Added to Rolls		Removed from Rolls[1]		End of Period			
Two-Year Period	Count	Annual Allowances	Count	Annual Allowances	Count	Annual Allowances	Count	Annual Allowances	% Increase in Annual Allowances	Average Annual Allowances
2003-2005	2,172	$54,687,000	398	$16,679,642	144	$2,070,047	2,426	$69,466,000	27.0%	$28,634
2001-2003	2,030	$45,208,000	313	$10,151,748	171	$503,802	2,172	$54,687,000	21.0%	$25,178
1999-2001	1,824	$37,137,000	230	$6,655,000	24	$268,000	2,030	$45,208,000	21.7%	$22,270
1997-1999	1,745	$32,630,000	202	$4,642,000	123	$1,514,000	1,824	$37,137,000	13.8%	$20,360
1995-1997	1,636	$29,029,000	190	$4,143,000	81	$946,000	1,745	$32,630,000	12.4%	$18,699

[1] This column consists of the following categories:
(a) Retirees and disabled retirees who die during the period and have no survior benefits.
(b) Expiration of certain period benefits for deceased retirees.

Solvency Test

July 1, 1995 to June 30, 2005

Year Ended	(1) Active Members Contributions	(2) Benficiaries Accrued Liability	(3) Retirants and Accrued Liability (Employer Portion)	Active Members Actuarial Value of Assets	Portion of Accrued Liabilities Covered by Reported Assets (1)	(2)	(3)
2005	$230,027,497	$824,042,723	$657,299,610	$1,384,454,000	100%	100%	50%
2003	$224,874,793	$635,092,039	$451,723,795	$1,280,719,017	100%	100%	93%
2001	$210,377,000	$529,853,000	$332,103,000	$1,060,144,000	100%	100%	96%
1999	$196,887,000	$441,573,000	$223,766,000	$804,860,000	100%	100%	74%
1997	$167,837,000	$383,574,000	$184,361,000	$678,954,000	100%	100%	69%
1995	$133,805,000	$364,159,000	$160,211,000	$566,102,000	100%	100%	43%

Actuarial Analysis of Financial Experience

For the Six-Year Period Ending June 30, 2005

	Change in Contribution Rate
For Plan Year Ended June 30, 2005	
Investment Performance	1.77%
Liability Experience	2.37%
Change in Assumptions	-0.59%
Change in Benefit Provisions	0.00%
TOTAL	**3.55%**
For Plan Year Ended June 30, 2003	
Investment Performance	2.78%
Liability Experience	2.60%
Change in Asset Valuation Method	-2.48%
Change in Assumptions	0.00%
Change in Benefit Provisions	0.00%
TOTAL	**2.90%**
For Plan Year Ended June 30, 2001	
Investment Performance	-0.46%
Liability Experience	-1.62%
Change in Assumptions	0.00%
Change in Benefit Provisions	1.51%
TOTAL	**-0.57%**
For Plan Year Ended June 30, 1999	
Investment Performance	-2.75%
Liability Experience	0.98%
Change in Assumptions	0.79%
TOTAL	**-0.98%**

Summary of Retirement Benefit Provisions

1. ***Eligibility:*** Members are eligible on their first day of City employment.

2. ***Final Compensation:*** Highest 12-month average salary, if separation takes place on or after July 1, 2001.

   Highest 36-month average salary, if separation takes place before July 1, 2001.

3. ***Service Retirement:***
   a) *Eligibility:* Age 55 with 5 years of service, or any age with 30 years of service.
   b) *Benefit:* 2.5% of Final Compensation for each year of service. Maximum benefit is 75% of Final Compensation.
   c) *Form of Payment:* Monthly benefit payable for the life of the member.

4. ***Disability Retirement:***
   a) *Eligibility:* Physically or mentally incapacitated so unable to perform duties of position. If disability is not service connected, then the member must have at least five years of City service.
   b) *Benefit:* 2.5% of Final Compensation per year of service. The maximum benefit is 75% and the minimum benefit is 40% of Final Compensation. Any Workers' Compensation benefits are offset from the benefits under this system.

      If the disability was non-service connected, then the benefit is reduced by .5% for every year under age 55.

      For those members who are hired on or after September 1, 1998, the non-service connected benefit is as follows:

      20% of Final Compensation for 6 years of service;

      Plus 2% for each years of service in excess of 6, but less than 16;

      Plus 2.5% for each year of service in excess of 16.
   c) *Form of Payment:* Monthly benefit payable for the life of the member.

5. ***Deferred Service Retirement:***
   a) *Eligibility:* Five years of membership prior to termination of City service. Member must leave contributions on deposit until retirement.
   b) *Benefit:* Same as Service Retirement, payable anytime after age 55.
   c) *Form of Payment:* Same as Service Retirement.

6. ***Pre-Retirement Death Benefits:***
   a) *Non-Service Connected with less than five years of service, or No Family Members Eligible for Allowance:* Member's beneficiary or estate receives (i), and (ii) where:

      (i) = Accumulated contributions with interest.

      (ii) = Lump sum benefit of one month's salary for each year of service, up to six years.
   b) *Service-Connected, or Non-Service Connected with five years of service:* Member's eligible survivor receives 2.5% of Final Compensation per years of service. The maximum benefit is 75% and the minimum benefit, if still an active employee at time of death, is 40% of Final Compensation, payable until the spouse remarries. If the Member was age 55 with 20 years of service at death, the benefit is payable for the lifetime of the Member's spouse.

7. ***Post-Retirement Death Benefits:*** Member's eligible survivor receives (i) and (ii), where:

   (i) = 50% continuance to surviving eligible spouse; if there is no surviving spouse, certain benefits are paid to the children.

   (ii) = $500 death benefit allowance for burial expenses at death of retired member.

8. ***Post-Retirement Cost-of-Living Benefits:***

   Each April 1, the benefits are increased by the percentage increase in CPI (to a maximum of 3%). Increases in CPI above 3% are "banked" to apply in years when CPI increase is less than 3%.

   The first cost-of-living adjustment is on the first day of the month following the one-year anniversary of retirement. The next adjustment will be prorated for the number of months remaining until the following April.

9. ***Employee Contributions:*** The Members' contribution rates are recalculated on an actuarial basis at each actuarial study. Contributions are credited with 3% interest annually (the interest crediting provision was changed from 7.25% to 3% effective July 1, 2001).

   All references to spouse also encompass registered domestic partners.

Summary of Health Subsidy Benefit Provisions

1. ***Eligibility:***
   a) *Medical:* Fifteen years of service credit at retirement, or receiving an allowance of at least 37 1/2% of Final Compensation. Must be enrolled in a City medical insurance plan at retirement.
   b) *Dental:* Five years of service credit at retirement, or receiving an allowance of at least 37 1/2% of Final Compensation. Must be enrolled in a City dental insurance plan at retirement.

2. ***Benefit:***
   a) *Medical:* The Retirement System pays 100% of the premium for the lowest cost medical plan offered by the City for single and family coverage. Members and eligible survivors pay for the difference in the premium for their selected plan and the portion paid by the Retirement System for the lowest cost plan.
   b) *Dental:* The Retirement System pays the entire cost of dental insurance coverage.

3. ***Contributions:*** Both the City and the Members contribute to the Retirement System fund for medical and dental insurance benefits.

Actuary Certification Letter

GRS Gabriel Roeder Smith & Company
Consultants & Actuaries

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September 14, 2007

Board of Administration
City of San José
Federated City Employees' Retirement System
1737 North First Street, Suite 580
San José, CA 95112-4505

RE: ACTUARIAL VALUATION CERTIFICATION

Dear Members of the Board:

The actuarial valuation report for the City of San Jose Federated City Employees' Retiree Health Care Plan, completed as of June 30, 2006, describes the current actuarial condition of the plan and determines the employer contribution rates necessary to fully support the benefits provided by the City of San Jose. This conclusion is based on financial and demographic data as of the valuation date and on current actuarial assumptions, which are based on the System's demographic and economic experience. This letter serves as the Actuary's certification letter and offers our independent actuarial review opinion.

In support of this opinion and certification, we have included the following information:

- The funding objective of the plan.
- The frequency of the plan's actuarial valuations and date of the most recent actuarial valuation.
- The source and degree of verification of the data used in the actuarial valuation.
- Supporting schedules that we have prepared and attached.
- The assumptions and methods used to value plan assets and liabilities relative to the Government Accounting Standards Board (GASB) Statement No. 45.

The Funding Objective of the Plan

The Governmental Accounting Standards Board (GASB) recently issued two accounting standards (GASB 43 and GASB 45) applicable to "Other Post-Employment Benefits," or OPEB plans such as the Retiree Health Care Plan offered by the City of San Jose. GASB Statement 45 relates to sponsors of OPEB plans while GASB 43 is applicable to the OPEB plan itself. This report has been completed in accordance with the implementation of these new standards.

The GASB standards require that the long-term cost of retiree health care and other OPEB benefits be determined and accrued on an actuarial basis similar to pension plans. The results of these valuations, including an annual OPEB expense (i.e. Annual Required Contribution, or ARC) and net obligation, would

Actuary Certification Letter *Continued*

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have to be disclosed on the City's financial statements. For a plan of this size, valuations are required to be prepared at least once every two years.

The GASB standards do not mandate the pre-funding of OPEB liabilities. However, any pre-funding of OPEB benefits either prior to or after the effective date of these new standards, will help minimize or eliminate the OPEB obligation that will be required to be disclosed in the State's financial statements. This net OPEB obligation would be required to be disclosed on the financial statements and could have a detrimental impact on the employer's perceived financial health.

This funding objective is currently being realized through contributions sufficient to pay the System's normal cost as well as amortizing unfunded liabilities over a combination of 30 years and the present value of future salaries.

The funded ratio (the ratio of the actuarial value of assets to the actuarial accrued liability) is a standard measure of a plan's funded status. In the absence of benefit improvements, it should increase over time, until it reaches 100%. Since the plan has been pre-funded prior to the implementation of these new standards, the current funded ratio is 12%.

The Frequency of the Plan's Actuarial Valuations and Date of the most Recent Actuarial Valuation

This plan is valued on at least a bi-annual basis, as of June 30. The most recent actuarial valuation was completed as of June 30, 2006.

The Source and Degree of Verification of the Data Used in the Actuarial Valuation

Computer files containing data on System membership of June 30, 2006 were provided by the City of San Jose Department of Retirement Services. While these files were not audited, the data was checked for internal consistency and was reviewed for reasonableness and consistency in relation to the data provided for the prior valuation.

Asset-related data were also received from the City of San Jose Department of Retirement Services and were used without further audit.

Supporting Schedules

We have prepared the following supporting schedules for inclusion in this Financial Statement:

- Summary of actuarial assumptions and methods
- Schedule of funding progress
- Schedule of employer contributions
- Summary of benefits provided by the retiree health benefit plan

Actuary Certification Letter *Continued*

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Actuarial Assumptions and Methods Used for Funding Purposes

The assumptions and methods used for funding purposes meet the parameters set for the disclosures presented in the financial section by Government Accounting Standards Board (GASB) Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions. In our opinion, the assumptions are reasonably related to past experience and represent our best estimate of future conditions affecting the System. Nevertheless, the emerging costs of the System will vary from those presented in this report to the extent actual experience differs from that projected by the actuarial assumptions.

Certification

We certify that the information presented herein is accurate and fairly portrays the actuarial position of the plan as of June 30, 2006. We prepared the accompanying Summary of Actuarial Assumptions and Methods, but the URS staff prepared the other supporting schedules in this section and the trend tables in the financial section based on information supplied in our report.

All of our work conforms with generally accepted actuarial principles and practices, and with the Actuarial Standards of Practice issued by the Actuarial Standards Board. In our opinion, our calculations also comply with the requirements of Utah state law and, where applicable, the Internal Revenue Code, ERISA, and the Statements of the Governmental Accounting Standards Board. The signatory is a Fellow of the Society of Actuaries, an Enrolled Actuary, and a Member of the American Academy of Actuaries with extensive experience in performing valuations for OPEB plans.

Sincerely,

Leslie L. Thompson

Leslie L. Thompson, FSA, EA, MAAA
Senior Consultant

Summary of Post-Employment Benefit Provisions Evaluated

ELIGIBILITY

Medical

Employees retiring (including deferred vested members) at age 55 with 15 years of service; or with a monthly pension equal to at least 37.5% of final average compensation.

Employees who become disabled and have a monthly pension equal to at least 37.5% of final average compensation.

Spouse/domestic partners of retired members who are qualified for medical are eligible to receive coverage if married and enrolled in one of the City's medical plans at the time of the member's retirement.

Dependent children under 19 years of age (24 if a full-time student) are eligible to receive coverage.

Surviving spouses/domestic partners/children of deceased members are eligible for coverage only if

- the employee has 15 years of service at the time of death or is entitled to a monthly pension of at least 37.5% of final compensation; and
- both the member and survivor are enrolled in a City medical insurance plan at the time of death; and
- the survivor will receive a monthly pension allowance.

Dental

Employees retiring or becoming disabled directly from City service must

- have 5 or more years of service; and
- is enrolled in one of the dental insurance plans sponsored by the City

Spouses/domestic partners/children are eligible to receive coverage if enrolled and married at the time of the member's retirement.

Surviving spouses/domestic partners/children of deceased members are eligible for coverage only if

- the employee has 5 years of service at the time of death; and
- both the member and survivor are enrolled in a City dental plan at the time of death; and
- the survivor will receive a monthly pension allowance.

BENEFITS

Medical

The Retirement System pays 100% of the premium for the lowest cost health plan available to active City employees. The member pays the difference if another plan is elected.

Effective January 1, 2006 the lowest cost health plan is Kaiser; family coverage is $939.72 and single coverage is $377.40 per month.

Dental

The Retirement System pays 100% of the dental insurance premiums.

RETIREE PREMIUM RATES

Monthly rates used for 2006 are shown below.

	Effective January 1, 2006	
MEDICAL	*Single*	*Family*
Non-Medicare Monthly Rates		
Kaiser – Traditional (CA)	$377.40	$939.72
Blue Shield HMO	$380.82	$978.22
Blue Shield POS or PPO	$563.58	$1,448.32
Supplemental Medicare Monthly Rate		
Kaiser – Senior Advantage	$342.08	$684.16
Secure Horizons – Medicare + Choice	$315.75	$631.50
PacifiCare – Senior Supplement Plan F	$257.00	$514.00
Blue Shield – Medicare PPO	$434.20	$868.40
Blue Shield – Medicare HMO	$284.84	$569.68

DENTAL	*Single*	*Family*
Delta Dental PPO	$97.84	$97.84
Delta Care PMI	$50.10	$50.10

Summary of Actuarial Assumptions and Methods

Basic Benefits. Normal cost and the allocation of benefit values between service rendered before and after the valuation date were determined using the entry age normal cost method.

Financing of Unfunded Actuarial Liability. The unfunded actuarial liability was amortized by level percent of payroll contributions over 30 years, the maximum period allowed under the GASB standards.

The expensing and benefit values of the Plan are calculated by applying actuarial assumptions to the benefit provisions and member information furnished, using the actuarial cost methods described above.

The principal areas of financial risk which require assumptions about future experiences are:

(1) long-term rates of investment return to be generated by the assets of the Fund.

(2) patterns of future medical inflation rates.

(3) rates of mortality among actives, retirants, and beneficiaries.

(4) rates of withdrawal of active employees (without entitlement to a retirement benefit).

(5) the age patterns of actual retirements.

In performing a valuation, the monetary effect of each assumption is calculated for as long as a present covered person survives – a period of time which can be as long as a century.

Actual experience of the system will not coincide exactly with assumed experience, regardless of the choice of the assumptions, the skill of the actuary and the precision of the many calculations made. Each valuation provides a complete recalculation of assumed future experience and takes into account all past differences between assumed and actual experience. The result is a continual series of adjustments (usually small) to the computed expense. From time to time it becomes appropriate to modify one or more of the assumptions, to reflect experience trends (but not random year-to-year fluctuations).

The annual rate has been computed to remain relatively level from year to year so long as benefits and the basic experience and make-up of employees do not change. Examples of favorable experiences which would tend to reduce the amount expensed are:

(1) Employee non-vested terminations at a higher rate than assumed.

(2) Mortality among retirees and beneficiaries at a higher rate than indicated by our mortality assumptions.

(3) Lower rates of medical inflation than assumed.

(4) Actual retirement ages higher than assumed.

The Entry Age Normal Actuarial Cost Method was used in this valuation.

The investment return rate used for the actuarial valuation is 5.6% per annum, compounded annually. This assumption is used to equate the value of payments due at different points in time.

The inflation rate used for the actuarial valuation calculations was 4.0% per year, compounded annually, the rate used in the City's pension valuation. It represents the difference between the investment return rate and the assumed real rate of return.

Payroll growth rate: 4%

Assumed future medical inflation. The valuation assumes that future medical inflation will be at a rate of 12% per annum graded down each year in 1% increments to an ultimate rate of 4.5% in 2014. Dental inflation is assumed to be 6% graded down to 4% over a nine-year period.

Date of Increase	*Assumed Medical Inflation*	*Assumed Dental Inflation*
12/31/2006	12.0%	6.0%
12/31/2007	11.0	6.0
12/31/2008	10.0	5.5
12/31/2009	9.0	5.5
12/31/2010	8.0	5.0
12/31/2011	7.0	5.0
12/31/2012	6.0	4.5
12/31/2013	5.0	4.5
12/31/2014 +	4.5	4.0

Rates of separation from active membership are shown below (rates do not include separation on account of retirement or death). This assumption measures the probabilities of members remaining in employment.

Sample Ages	*Disability**	*Withdrawal*	*Vested Termination*
20	.04%	11.00%	--- %
25	.06	7.00	3.00
30	.07	5.00	3.00
35	.09	2.50	2.75
40	.15	1.50	2.00
45	.25	1.25	2.00
50	.40	1.25	1.50
55	.50	1.00	0.00
60	1.00	1.00	0.00
65	2.00	0.00	0.00
70	0.00	0.00	0.00

**50% of the disabilities are assumed to be duty-related and 50% are assumed to be non-duty related.*

For inactive members, the assumed age at retirement is age 58.

The post-retirement mortality table used for healthy retirees and beneficiaries was the 1994 Group Annuity Mortality Table (sex distinct). The disabled mortality table used was the 1981 Disability Mortality Table. This assumption is used to measure the probabilities of members dying after retirement and the probabilities of each benefit payment being made after retirement. Sample values are shown below.

	Future Life Expectancy *(Years)*			**% of Benefit Recipients Dying Each Year**		
Sample Ages	*Retired Men*	*Retired Women*	*Disabled*	*Retired Men*	*Retired Women*	*Disabled*
45	35.4	39.7	23.6	0.16%	0.10%	2.08%
50	30.7	34.9	21.1	0.26	0.14	2.44
55	26.2	30.2	18.7	0.44	0.23	2.84
60	21.8	25.6	16.4	0.80	0.44	3.30
65	17.8	21.3	14.1	1.45	0.86	3.79
70	14.3	17.3	11.7	2.37	1.37	4.37
75	11.1	13.6	9.2	3.72	2.27	5.53
80	8.4	10.3	7.0	6.20	3.94	8.74

Summary of Actuarial Assumptions and Methods *Continued*

The active member mortality assumption measures the probability of mortality before retirement. The rates include probability of ordinary death, service death, and death while eligible for retirement or disability.

% of Active Members Dying Each Year

Sample Ages	Men	Women
30	.06%	.05%
35	.06	.05
40	.07	.06
45	.09	.08
50	.16	.13
55	.26	.20
60	.38	.30
65	.53	.44

The rates of retirement used to measure the probability of eligible active members retiring during the next year.

Retirement Ages	% of Active Members Retiring Within the Next Year	Retirement Ages	% of Active Members Retiring Within the Next Year
55	15.0%	63	10.0%
56	7.5	64	10.0
57	7.5	65	25.0
58	7.5	66	25.0
59	7.5	67	25.0
60	7.5	68	25.0
61	7.5	69	25.0
62	20.0	70	100.00

**Superceded by 50% retirement probability each year after completion of 30 years of service and attainment of age 50.*

Additional Medical Assumptions

The eligibility conditions for retiree medical coverage we used were after attainment of age 55 and 15 years of service at retirement, or a monthly pension equal to 37.5% of final average compensation. Deferred retirements and disabled retirements meeting this requirement are also eligible for medical coverage. The eligibility condition for medical coverage for future surviving spouses was assumed to be the active member's attainment of 15 years of service.

Participation in retiree medical plans: We assume 85% of future retirees meeting the eligibility conditions above will participate in the retiree medical plan.

The probability of electing spouse/domestic partner coverage at retirement was assumed to be 55% for future retirees, with males assumed to be three years older than their spouses, and females assumed three years younger. Also, 55% of active members dying in service are assumed to leave surviving spouses who elect medical coverage. 100% of surviving spouses of retired members are assumed to continue coverage.

Additional Dental Assumptions

The eligibility conditions for retiree dental coverage we used were after attainment of 5 years of service at retirement, or eligible for disabled retirement. Deferred retirements are not eligible for dental coverage. The eligibility condition for dental coverage for future surviving spouses was assumed to be the active member's attainment of 5 years of service.

Participation in retiree medical plans: We assume 100% of future retirees meeting the eligibility conditions above will participate in the retiree dental plan.

The probability of electing spouse/domestic partner coverage at retirement was assumed to be 65% for future retirees, with males assumed to be three years older than their spouses, and females assumed three years younger. Also, 65% of active members dying in service are assumed to leave surviving spouses who elect medical coverage. 100% of surviving spouses of retired members are assumed to continue coverage.

Implicit Subsidy and Premium Development: Premium development is required for the two classes of retirees (pre-age 65 and post-age 65). These premiums were developed using fully-insured premium rates from the health plans offered in conjunction with census data for the active and retired participants of the City's medical benefit plan (see pages 25 and 26). These premium rates were adjusted to reflect the increase in utilization expected of an older population and the decrease in expected number of dependents covered under family coverage. In addition, these premium rates were adjusted to reflect differing utilization rates by age and sex. Sex-specific aging factors used reflect the expectation that women will have about the same per capita claims as men at age 57 years, have higher claims before age 57, and have lower claims after age 57. Gross imputed single coverage rates at sample ages are shown below.

The impact of the recently enacted Federal legislation creating a prescription drug benefit under Medicare has not been reflected in this report since the impact will affect contributions (in the form of on-behalf contributions), not liabilities of the plan (GASB Technical Bulletin 2006-1).

GROSS IMPUTED SINGLE COVERAGE MONTHLY PREMIUM RATES BY AGE

Pre-Age 65 Retiree Rates			Post-Age 65 Retiree Rates		
Age	Male	Female	Age	Male	Female
55	$473.77	$486.99	65	$335.48	$308.93
60	595.19	572.10	70	386.97	347.96
64	692.77	642.13	75	429.60	381.26
			80	460.62	406.02

Dental Premium: Based on census data for current retiree dental plan participants (see page 25); we assumed 97% of future eligible retirees would choose Delta Dental PPO and 3% of future eligible retirees would choose Delta Care PMI. This produced a monthly dental premium rate of $90.50.

Funding Progress Indicators

There is no single all-encompassing indicator which measures a retirement system's funding progress and current funded status. A traditional measure has been the relationship of valuation assets to unfunded actuarial accrued liability – a measure that is influenced by the choice of actuarial cost method.

We believe a better understanding of funding progress and status can be achieved using the following indicators which are independent of the actuarial cost method.

(1) ***The ratio of assets to the actuarial present value of credited projected benefits*** allocated in the proportion accrued service is to projected total service – a plan continuation indicator. The ratio is expected to increase in the absence of benefit improvements or strengthening of actuarial assumptions.

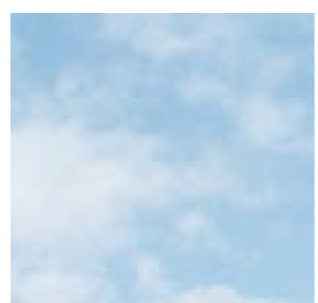
(2) ***The ratio of the unfunded actuarial present value of credited projected benefits to member payroll*** – a plan continuation indicator. In a soundly financed retirement system, the amount of the unfunded actuarial present value of credited projected benefits will be controlled and prevented from increasing in the absence of benefit improvements or strengthening of actuarial assumptions. However, in an inflationary environment, it is seldom practical to impose this control on dollar amounts which are depreciating in value. The ratio is a relative index of condition where inflation is present in both items. The ratio is expected to decrease in the absence of benefit improvements or strengthening of actuarial assumptions.

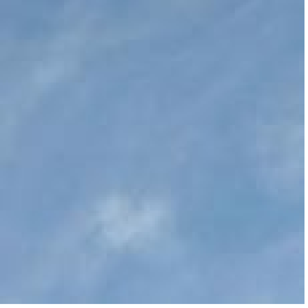
SCHEDULE OF FUNDING PROGRESS FOR RETIREE MEDICAL BENEFITS

Actuarial Valuation Date	*Actuarial Value of Assets (a)*	*AAL (b)*	*UAAL (b-a)*	*Funding Ratio (a/b)*	*Payroll (c)*	*UAAL as % of Payroll ((b-a)/c)*
6/30/06	$81,288,000	$702,938,665	$621,650,665	11.6%	$275,558,882	225.6

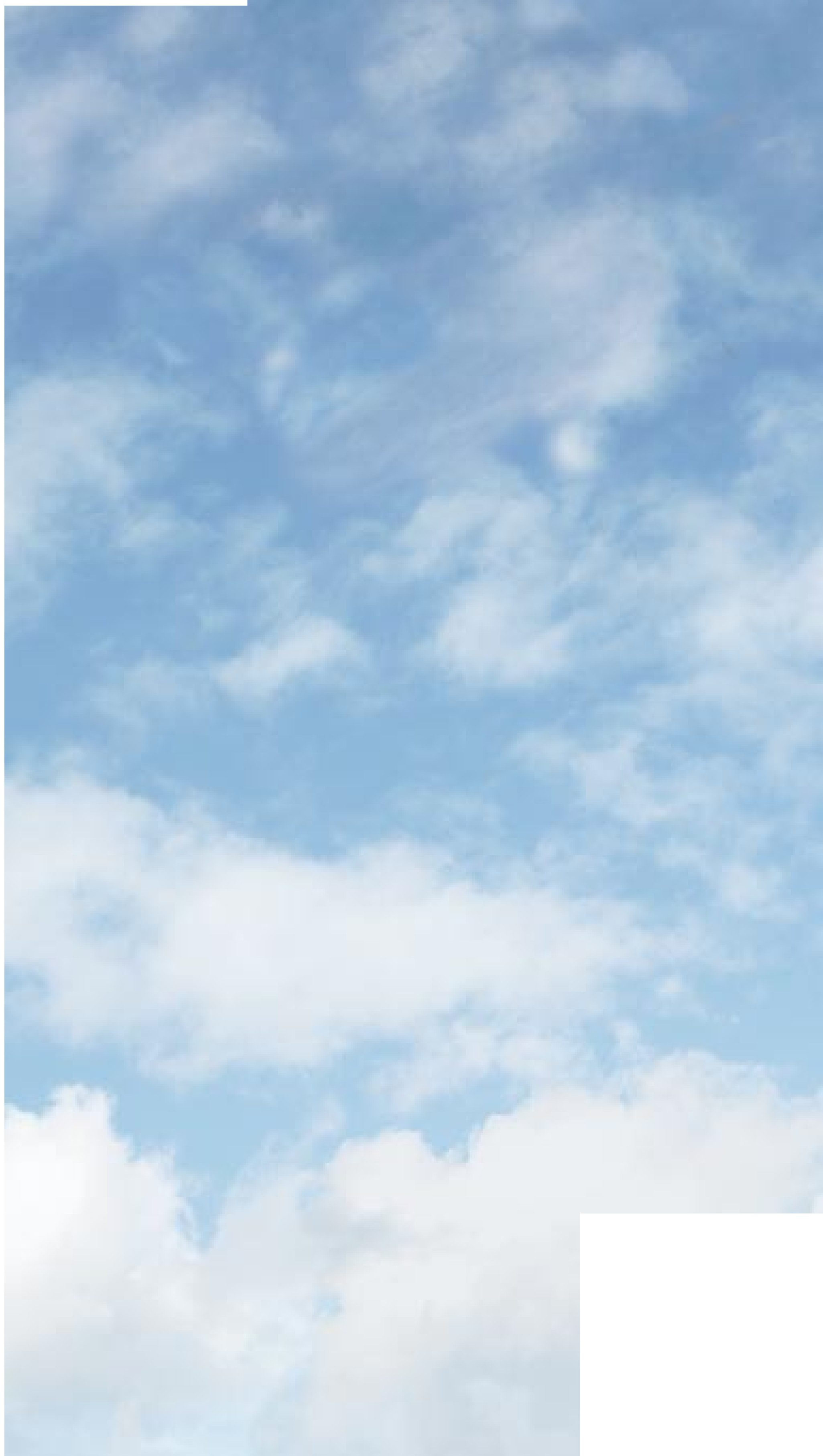
EMPLOYER CONTRIBUTIONS RETIREE MEDICAL BENEFITS ONLY

Year Ended	*Annual Required Contribution*	*Percentage Contributed*
June 30, 2007	$38,526,038	32%





Statistical Section



Statistical Review

CHANGES IN NET ASSETS FOR FISCAL YEARS 1998-2007 *(Dollars in thousands)*

Pension Benefits (Schedule 1a)

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Additions										
Member contributions	$9,078	$8,812	$10,804	$10,306	$11,071	$11,776	$12,394	$12,393	$12,395	$12,370
Employer contributions	30,367	30,139	34,146	35,284	41,011	38,411	39,534	41,552	41,267	51,004
Investment Income*	130,414	93,491	73,839	(2,934)	(24,140)	71,179	192,373	115,618	132,873	244,210
Total additions	**169,859**	**132,442**	**118,789**	**42,656**	**27,942**	**121,366**	**244,301**	**169,563**	**186,535**	**307,584**
Deductions (See Schedule 2a)										
Benefit payments	32,035	34,846	44,655	43,761	48,235	46,814	53,578	60,438	68,438	75,135
Death benefits	84	47	20	105	22	4,752	5,454	5,437	5,721	5,867
Refunds	1,980	646	1,386	1,886	1,207	714	1,188	927	1,246	1,008
Administrative expenses and other	782	682	1,059	1,322	1,378	1,532	1,799	1,588	1,790	1,845
Total deductions	**34,881**	**36,221**	**47,120**	**47,074**	**50,842**	**53,812**	**62,019**	**68,390**	**77,195**	**83,855**
CHANGE IN NET ASSETS	**$134,978**	**$96,221**	**$71,669**	**$(4,418)**	**$(22,900)**	**$67,554**	**$182,282**	**$101,173**	**$109,340**	**$223,729**

**Net of Expenses*

Postemployment Healthcare Benefits (Schedule 1b)

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Additions										
Member contributions	$2,051	$1,921	$1,679	$1,462	$2,787	$3,032	$3,191	$5,219	$5,226	$9,612
Employer contributions	2,326	2,248	1,596	1,750	4,127	3,866	3,948	5,996	5,961	10,728
Investment Income*	10,514	6,416	4,132	(536)	(1,558)	4,193	11,066	6,539	7,273	13,343
Total additions	**14,891**	**10,585**	**7,407**	**2,676**	**5,356**	**11,091**	**18,205**	**17,754**	**18,460**	**33,683**
Deductions (See Schedule 2b)										
Health Insurance Premiums	4,161	4,711	5,236	6,530	7,804	9,191	11,438	13,393	15,904	18,265
Administrative expenses and other	59	44	77	98	94	99	114	95	103	105
Total deductions	**4,220**	**4,755**	**5,313**	**6,628**	**7,898**	**9,290**	**11,552**	**13,488**	**16,007**	**18,370**
CHANGE IN NET ASSETS	**$10,671**	**$5,830**	**$2,094**	**$(3,952)**	**$(2,542)**	**$1,801**	**$6,653**	**$4,266**	**$2,453**	**$15,313**

**Net of Expenses*

Source: Pension Administration System

Statistical Review *Continued*

BENEFIT AND REFUND DEDUCTIONS FROM NET ASSETS BY TYPE *(Dollars in thousands)*

Pension Benefits (Schedule 2a)

Type of Benefit	*2007*	*2006*
Age and Service Benefits		
Retirees - Service	$64,978	$59,391
Retirees - Deferred Vested	4,860	4,134
Survivors - Service	3,320	3,195
Survivors - Deferred Vested	108	87
Death in Service Benefits	1,722	1,750
Disability Benefits		
Retirees - Duty	2,920	2,702
Retirees - Non-Duty	1,737	1,640
Survivors - Duty	197	187
Survivors - Non-Duty	519	502
Ex-Spouse Benefits	640	571
TOTAL BENEFITS	**$81,002**	**$74,159**
Type of Refund		
Separation	$1,008	$1,246
TOTAL REFUNDS	**$1,008**	**$1,246**

Fiscal Year 2004-05 data not available due to system limitations

Postemployment Healthcare Benefits (Schedule 2b)

Type of Benefit	*2007*	*2006*
Age and Service Benefits		
Retirees – Service		
Medical	$12,029	$10,341
Dental	2,022	1,870
Retirees – Deferred Vested		
Medical	767	652
Dental	35	-
Survivors – Service		
Medical	730	628
Dental	251	235
Survivors – Deferred Vested		
Medical	9	11
Dental	-	-
Death in Service Benefits		
Medical	313	293
Dental	72	71
Disability Benefits		
Retirees – Duty		
Medical	1,098	956
Dental	145	131
Retirees – Non-Duty		
Medical	478	433
Dental	78	73
Survivors – Duty		
Medical	69	59
Dental	18	17
Survivors – Non-Duty		
Medical	119	103
Dental	32	31
Ex-Spouse Benefits		
Medical	-	-
Dental	-	-
TOTAL BENEFITS	**$18,265**	**$15,904**

** Deferred Vested dental data unavailable in 2006*

Source: Pension Administration System

Statistical Review *Continued*

EMPLOYER AND EMPLOYEE CONTRIBUTION RATES FOR FISCAL YEARS 1998-2007 (Schedule 3)

Fiscal Year	*Employee Rate (%)*	*Employer Rate (%)*
1998*	5.31	16.52
1999	5.31	16.52
2000	5.31	16.52
2001	4.76	16.09
2002	4.96	17.40
2003	5.08	15.20
2004	5.08	15.20
2005	6.06	17.12
2006	6.06	17.12
2007	7.58	21.98

* *Multiple rates this year*

Source: Pension Administration System

Retired Members by Type of Benefit

PENSION BENEFITS *As of June 30, 2007*

Monthly Benefit Amount	*Number of Retirees & Beneficiaries*	***Type of Retirement**** *1*	*2*	*3*	*4*	*5*	*6*	***Option Selected***** *A*	*B*	*C*	*Total*
$1 - 500	168	57	45	2	-	11	53	79	19	70	168
501 - 1000	311	111	101	5	4	26	64	138	13	160	311
1001 - 1500	372	148	116	25	22	2	59	193	27	159	379
1501 - 2000	363	215	47	34	25	12	30	219	30	107	356
2001 - 2500	332	219	39	34	14	4	22	219	19	94	332
2501 - 3000	268	216	10	14	10	2	16	189	23	56	268
3001 - 3500	218	188	8	8	1	-	13	147	21	50	218
3501 - 4000	203	182	6	3	2	1	9	162	14	27	203
4001 - 4500	149	139	4	1	-	-	5	100	15	33	148
4501 - 5000	110	107	-	-	-	-	3	76	9	26	111
Over $5000	255	245	-	3	-	-	7	197	18	40	255
TOTAL	**2749**	**1827**	**376**	**129**	**78**	**58**	**281**	**1719**	**208**	**822**	**2749**

***RETIREMENT CODES**

1 Service
2 Survivor
3 Service-Connected Disability
4 Non-Service-Connected Disability
5 Ex-Spouse
6 Deferred Vested

****OPTION DESCRIPTIONS**

A Unmodified - 50% Continuance
B Option 1 - 100% Continuance/reduced pension
C No Survivor - No Continuance

POSTEMPLOYMENT HEALTHCARE BENEFITS

Amount Monthly Benefit	***Type of Subsidy*** *Health*	*Dental*
Ineligible/Deferred	726	399
$1 - 60	-	65
61 - 250	1	2285
251 - 500	951	-
501 - 750	35	-
751 - 1000	1036	-
TOTAL	**2749**	**2749**

Source: Pension Administration System

Average Benefit Payment Amounts

PENSION BENEFITS

	Years of Service Credit						
	0-5	6-10	11-15	16-20	21-25	26-30	31+
Retirement Effective Dates							
Period 7/1/2006 to 6/30/2007							
Average Monthly Benefit*	$ 732	$1,049	$1,728	$2,398	$3,129	$4,352	$4,947
Average Final Average Salary	$3,455	$3,627	$3,867	$4,316	$4,263	$5,030	$5,505
Number of Retired Members**	115	307	344	476	342	564	105
Period 7/1/2005 to 6/30/2006							
Average Monthly Benefit*	$ 665	$ 981	$1,638	$2,252	$2,971	$4,142	$4,673
Average Final Average Salary	$3,073	$3,413	$3,704	$4,123	$4,067	$4,755	$5,324
Number of Retired Members**	116	294	337	449	322	536	100

* *Includes Cost of Living Increases*

** *Does not include Survivors and Ex-Spouses Information presented in the above table is not readily available prior to fiscal year 2006.*
Information presented in the above table is not readily available prior to fiscal year 2006.

POSTEMPLOYMENT HEALTHCARE BENEFITS

	Years of Service Credit						
	0-5	6-10	11-15	16-20	21-25	26-30	31+
Retirement Effective Dates							
Period 7/1/2006 to 6/30/2007							
Average Health Subsidy	$728	$683	$654	$678	$679	$736	$700
Number of Health Participants*	23	45	195	459	331	555	104
Average Dental Subsidy	$ 97	$ 97	$ 97	$ 97	$ 97	$ 97	$ 97
Number of Dental Participants*	62	202	286	431	318	552	105
Period 7/1/2005 to 6/30/2006							
Average Health Subsidy	$616	$635	$613	$614	$615	$670	$641
Number of Health Participants*	24	49	189	416	305	520	98
Average Dental Subsidy	$ 95	$ 94	$ 94	$ 94	$ 94	$ 94	$ 94
Number of Dental Participants*	62	191	280	397	297	521	99

* *Does not include Survivors and Ex-Spouses*
Information presented in the above table is not readily available prior to fiscal year 2006.

Source: Pension Administration System

Retirements During Fiscal Year 2006-07

SERVICE RETIREMENTS

AGUIRRE, DAVID
ALBANO, JOSE
ALDAMA, FELIPE
ALDERETE, JIM
ALFORD, NANCY
ALLISON, WINIFRED
ALTAMIRANO, JOSEPH
ALTSTADT, DAVID
ANDERSON, HEIDI
ANDERSON, MICHAEL
ANTONOWICZ, GERMAINE
ATCHISON, DOROTHY
ATKINS, ETHEL
BANKO, NANCY
BAUM, BETTY
BELVILLE, DENNIS
BENGIVENO, WILLIAM
BOSCH, MARY
BROWN, JERRY
BRUINSMA, DANIEL
CABRAL, MARY
CALUZA, PURIFICACION
CANO, JULIE
CARDINALLI, JOSEPH
CARROLL, GREG
CASTRO, CARMEN
CASUGA, FRED
CHANDRASEKHAR, KAMALA
CHARFAUROS, JOSEPH
CLEVELAND, OLGA
CORDERO, EMMANUELLE
COX, JANELLE
CRUZ, PEDRO
DAVIS, ALBERT
DECKER, ALAN
DIXON, MARIAN
DIZON, ROGELIO
DORSA, SHIRLEY
DUCKWORTH-LANZO, MARCIA
DUNCAN, GEORGIANNA
DYKE, JACK
EDMONDS, MICHAEL
FRANKLIN, MARY
FROMAN, MARY
GARNER, RONALD
GEBHARDT, CHARLES
GURARO, JOHN
HAMILTON, PAUL
HARRISON, MONROE
HEMMEN, NANCY
HERNANDEZ, GEORGE
HO, ANITA
HOLCOMB, ALETA
HORIO, MARY
HORTON, DEBRA
HUBBARD, GARY
JEZO, PATRICIA
JOHNSON, DIANE
JOHNSON, ROBERT
JOHNSTON, LAURA
KOBAYASHI, BONNIE
KONDO, K JEANNE
KWONG, MAY
LEDESMA, STEPHEN
LEIGH, DOROTHY
LIAO, LIH
LIPARI, VICTOR
LISENBEE, LARRY
LUPTON, SUSAN
MANNINA, DIANE
MARIDON, LINDA
MARTINEZ, ARTHUR
MAYNE, DEBORAH
MCFADDEN, DANIEL
MELCHOR, MANUEL
MENDOZA, MARYLOU
MYHRE, BROOKE
NAKAI, LINDA
NELSON, NADINE
NOSTRAND, RITA
OLIVA, JOSE
OVERTON, EDWARD
PALMER, DENNIS
PARADA, CRAIG
PATONAI, RICHARD
PEREZ, ALBERT
PHAM, KIMDUNG
PHARR, LAWRENCE
PHILIBOSIAN, MICHELE
PICKETT, LARRY
POOLER, JAMES
POWELL, DEBORAH
PRITCHARD, NANCY
PUNSALAN, RENATO
RIOS, CATHERINE
RIOS, JOSE
RODARTE, FRANK
RODRIGUEZ, CESARIO
ROWLETT, LINDA
RUIZ, MARIA
SAADATI, TAGHI
SALAZAR, MARIA
SANTOMAURO, RANDY
SEPULVEDA CONTE, ELEANOR
SEQUEIRA, ADOLFO
SHEPARD, DEBBIE
SHKAPSKY, CONSTANTINE
SILVA, MACLEEN
SIMONS, WILLIAM
SKENE, CAROLYN
SMERZ, GERALD
SNOW, SHARON
SPEED, WILLIAM
STANDRIDGE, LLOYD
STANLEY, GEORGE
STANTON, JAMES
STEVENS, EARL
STEVENS, ROBERT
STOVALL, BRIAN
STULTS, ANN
SZEGEDY, GABOR
TSUCHIMOTO, ELIZABETH
TUCKER, WILLIAM
VALERIO, CARMENCITA
VILLARREAL, JUAN
VILLEGAS, JULIO
WAKAYAMA, KAZUO
WALKER, THERESA
WEICHERT, ELAINE
WILLIAMS, THOMAS
WILLIAMSON, KATHLEEN
YAU, RICHARD
YOSHIOKA, STANLEY
ZARATE, DIANE

Source: Pension Administration System

Retirements During Fiscal Year 2006-07 *Continued*

DEFERRED VESTED RETIREMENTS

BROWN, HOLLY
BURNETT, CHRISTINE
BURROUGHS, BRUCE
CARRIVEAU, PATRICIA
CLARKE, DAVID
CODY, BONNIE
FLATLEY, MARY
GALINDO, EULALIO
GUERRERO-DALEY, TERESA
GUFFEY, JAN
KERN, JANET
LISS, GARY
MACY, CYNTHIA
MENDOZA, MANUEL
MORA, MARILY
OLIVER, KENNETH
RICHMOND, ELAINE
RODRIGUEZ, ELODIA
ROSE, WANDZIA
SCOTT, WILLIAM
SHIPES, RANDOLPH
SKALLAND, SHARON
STANG, SANDRA
STOLLMEYER, PAULA
STOWELL, GARY
TAMAYO, MANUEL
YOSHINO, STEVE

SERVICE-CONNECTED DISABILITY RETIREMENTS

NONE

NON-SERVICE-CONNECTED DISABILITY RETIREMENTS

HAIDER, FAZILAT
MENDEZ, RAY

Deaths During Fiscal Year 2006-07

DEATHS AFTER RETIREMENT

AKROP, ANNE
ALLEN, L RHEDA
BAGLEY, WALTER
BISHOP, EDWARD
BURNELL, VIRGINIA
CHANCE, BEVERLY
CHRISTIAN, PAUL
CLARE, PHYLLIS
CLEGHORN, ERNESTINE
COLLIER, VIRGINIA
COON, ROBERT
COX, MILTON
CULBERTSON, PATRICIA
CURTIS, EDWARD
D'ALESSANDRIA, LUIS
DUNKLE, MARJORIE
EATON, DAVID
EIGUREN, PETE
FARNSWORTH, MARGUERITE
HALL, EARL
JONES, KENNETH
JONES, LUCILLE
JUNCK, NAJOO
KATAYAMA, TSUNEO
KRENZ, CARROLL
LEVANDOWSKI, HERBERT
LIBBY, RALPH
LONG, THOMAS
LOWE, JAMES
MAASEN, DIRK
MARTINEZ, GILBERT
MATTHEWS, DONNALEE
MATUSIEWICZ, THADDEUS
MC CLURE, ALLEN
MC GOWAN, THOMAS
MC MURRAY, KATHRYN
MIURA, AKIO
NIGRO, DOROTHY
O'HEARN, PATRICIA
POTTER, GRACE
ROCK, PAULA
SANDOVAL, CONSTANCE
SANDOVAL, PETER
SCHRULL, ELSIE
SMITH, LAWRENCE
STEENFOTT, JOYCE
TENNIS, VIRGINIA
VALDEZ, ANSELMO
WARRINER, EDWARD
WHITTAKER, JOHN
WILLIAMS, THOMAS
WILSON, ANNA
WOLFF, VIRGINIA
WOOD, AVELINA
WOOD, DELBERT
YAU, HENRY
YOUNG, BETTY

DEATHS BEFORE RETIREMENT

AGUIRRE, GEORGE
DAVISON, ALMA R
RILEY, LINDA M
RIVAS, ROSALINDA

Source: Pension Administration System

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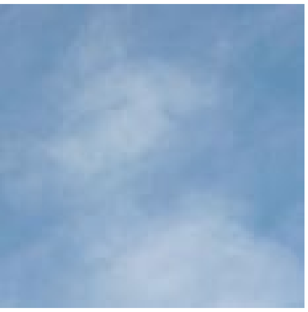

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