

DALLAS POLICE AND FIRE PENSION SYSTEM

**Financial Statements
and
Required Supplemental Information**

December 31, 2005 and 2004
(With Independent Auditors' Report Thereon)

DALLAS POLICE AND FIRE PENSION SYSTEM

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INDEPENDENT AUDITORS' REPORT

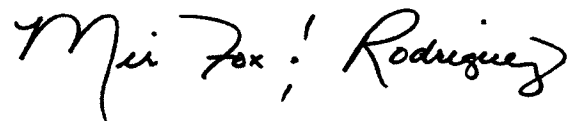
To the Board of Trustees
Dallas Police and Fire Pension System:

We have audited the accompanying statements of plan net assets of the Dallas Police and Fire Pension System (the System) as of December 31, 2005 and 2004, and the related statements of changes in plan net assets for the years then ended. These basic financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these basic financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the 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 audits provide a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial status of the System as of December 31, 2005 and 2004, and the changes in its financial status for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Management's discussion and analysis (MD&A) and the required supplemental information (schedules 1 and 2), are not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the MD&A and required supplemental information. However, we did not audit such information and do not express an opinion it.



August 7, 2006

MANAGEMENT'S DISCUSSION AND ANALYSIS (Unaudited)

OVERVIEW

The Management's Discussion and Analysis (MD&A) of the Dallas Police and Fire Pension System's (the System) financial position and performance provides an overview of the System's financial activities for the fiscal years ended December 31, 2005 and 2004. The System is a defined benefit pension plan. Certain comparative information between the current year and the prior year is required to be presented in the MD&A. The analysis should be read in conjunction with the Introductory Section of the annual report, the basic financial statements, notes to the basic financial statements and required supplementary information.

FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the System's financial statements which consist of (1) Basic Financial Statements and (2) Notes to Basic Financial Statements, including supplemental information.

The *Statement of Plan Net Assets* presents the System's assets and liabilities and plan net assets held in trust for the payment of pension benefits. The *Statement of Changes in Plan Net Assets* summarizes additions to and deductions from System assets, providing plan net assets held in trust at the end of the year for pension benefits. The difference between assets and liabilities is one measure of the System's financial position and the change in this measure over time is an indication of whether the System's financial health is improving or deteriorating.

The *Notes to Basic Financial Statements* provide additional information that is essential to a full understanding of the data provided in the Basic Financial Statements.

The System presents its financial statements solely on the accounts of the System. The accrual basis of accounting is used by the System, whereby revenues are recognized when they are earned and collection is reasonably assured, and expenses are recognized when the liability has been incurred. Investments are reported at fair value.

The required supplemental information consists of schedules of funding progress and employer contributions.

CONDENSED FINANCIAL INFORMATION

(in thousands)

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Assets	\$ 3,281,804	2,712,238	2,480,812
Liabilities	546,070	218,435	297,753
Plan Net Assets Available for Benefits	2,735,734	2,493,804	2,183,059
Contributions	105,122	100,646	94,610
Investment and Other Income	252,204	317,192	528,198
Benefit Payments	111,331	103,394	96,246
Withdrawal Payments and Refunds of Contributions	1,070	801	584
Administrative Expenses and Professional Fees	2,995	2,898	3,165

Continued

FINANCIAL HIGHLIGHTS

- The System's plan net assets increased by \$241.9 million in 2005 and by \$310.1 million in 2004. Plan net assets were \$2.74 billion in 2005 and \$2.49 billion in 2004. The increase reflects the income from employee and employer contributions and earnings on investments that exceeded benefit payments and administrative expenses.
- The rate of return on System investments during 2005 was 10.3%, net of fees, compared to a rate of return of 14.77% for 2004. The actuarial expected rate of return for both years was 8.5%.
- Liabilities totaled \$546.1 million as of December 31, 2005 compared to \$218.4 million as of December 31, 2004.
- The System received employee contributions of \$17.7 million in 2005 and \$17.4 million in 2004 and received employer contributions from the City of Dallas in the amounts of \$87.4 million and \$83.3 million in 2005 and 2004, respectively. The employee contributions are 8.5% of computation pay (base pay rate plus education and longevity pays). The employer contributions represent 27.5% of total salary and wages for covered employees.
- The System paid \$111.3 million in service retirement, disability retirement and survivor benefits and DROP disbursements during the year, compared to payments of \$103.4 million benefits in 2004. The System refunded approximately \$1.07 million and \$801 thousand in contributions to former members in 2005 and 2004, respectively. No changes to benefit provisions were implemented. The increase in benefit payments resulted both from an increase in the number of benefit recipients and annual adjustment increases to base benefits of 4%.
- The cost of administering the benefit programs of the System, including administrative costs and professional fees was nearly the same at \$2.9 million in 2005 compared to \$2.9 million in 2004.

FUNDING PROGRESS

The System contracted with Buck Consultants to conduct an actuarial valuation to determine the actuarial position of the System as of January 1, 2006. The Actuarial Valuation Report indicated that the overall funding of the System remains sound and the current contribution rates are sufficient to keep the System actuarially sound. In preparing the valuation, the actuary uses a smoothing process over a rolling five-year period of investment data to remove year-to-year volatility in asset returns.

- The Actuarial Valuation Report shows that the market value of assets increased \$261 million during the year to \$2.75 billion as of January 1, 2006. The market value of assets as of January 1, 2005 was \$2.49 billion. During the same period, the actuarial value of the assets (AVA) increased \$215.1 million to a total of \$2.70 billion as of January 1, 2006. For the January 1, 2005 valuation, the AVA was set equal to the market value of assets.
- As of January 1, 2006, the actuarial value of liabilities (AAL) increased by \$208.2 million to \$3.28 billion.
- The ratio of a plan's AVA to AAL, expressed as a percentage, is an indicator of the plan's funding status. Generally, the larger the percentage, the stronger the financial health of the plan. The System's AAL ratio improved to 82.3% as of January 1, 2006. The ratio as of January 1, 2005 was 80.8%.

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- When a plan's total liabilities exceed the assets available to pay benefits on an actuarial basis, the plan is said to have an unfunded actuarial accrued liability (UAAL). As of January 1, 2006, the System's UAAL was \$582.1 million, a decrease of \$7 million from a UAAL of \$589.1 million as of January 1, 2005.
- Another measure of funding status is funding period. This is the length of time in years needed to amortize the current unfunded actuarial accrued liability (UAAL) based on the current contribution rate. As of January 1, 2006, the employer contribution rate of 27.5% covers the normal cost and the amortization of the UAAL over 20 years, compared to 29 years to fund as of the January 1, 2005 valuation. This decrease of 9 years in the number of years to fully fund the System further demonstrates the improvement in the System's funding status.

CONTACTING THE SYSTEM'S FINANCIAL MANAGEMENT

This Financial Section is designed to provide our members and other users with a general overview of the System's financial activities. If you have questions about this report or need additional financial information, contact the Administrator of the Dallas Police and Fire Pension System at 2301 N. Akard Road, Suite 200, Dallas, TX 75201.

DALLAS POLICE AND FIRE PENSION SYSTEM

Statements of Plan Net Assets December 31, 2005 and 2004

<u>Assets</u>	<u>2005</u>	<u>2004</u>
Investments, at fair value (notes 2, 3 and 4):		
Cash and short term investments	\$ 272,737,505	288,678,041
United States government securities	21,086,315	20,234,022
United States government sponsored enterprises	34,239,013	8,700,000
Foreign government securities	247,540,762	193,837,110
Commingled funds	89,005,318	373,501,808
Domestic equities	831,471,786	501,582,329
International equities	660,850,977	598,469,171
Corporate securities	373,824,612	306,908,250
Investments, at appraised value - real estate equity funds	<u>546,201,086</u>	<u>383,872,834</u>
Total investments	<u>3,076,957,374</u>	<u>2,675,783,565</u>
Receivables:		
Accrued interest and dividends	12,335,285	10,896,980
Employer contributions (note 5)	1,025,927	997,588
Member contributions	203,027	206,778
Forward currency contracts (note 6)	77,540,182	763,258
Securities sold	<u>113,742,075</u>	<u>23,590,273</u>
Total receivables	<u>204,846,496</u>	<u>36,454,877</u>
Total assets	<u>3,281,803,870</u>	<u>2,712,238,442</u>
<u>Liabilities and Net Assets</u>		
Repurchase loan agreement (note 7)	51,778,137	7,060,000
Payable for securities purchased	106,224,192	41,984,780
Administrative and professional fees payable	14,606,635	3,690,480
Forward currency contracts (note 6)	79,254,983	771,437
Securities lending collateral (note 4)	207,815,275	164,927,817
Line of credit (note 8)	<u>86,390,791</u>	<u> </u>
Total liabilities	<u>546,070,013</u>	<u>218,434,514</u>
Net assets held in trust for pension benefits (a schedule of funding progress is included on page 24)	<u>\$ 2,735,733,857</u>	<u>2,493,803,928</u>

See accompanying notes to basic financial statements.

DALLAS POLICE AND FIRE PENSION SYSTEM

Statements of Changes in Plan Net Assets Years Ended December 31, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Additions to plan net assets:		
Investment income:		
Interest	\$ 32,011,489	27,774,638
Dividends	30,282,985	20,533,867
Real estate income	23,745,204	13,543,892
Net appreciation in fair value of investments	185,660,666	265,912,580
Securities lending income	2,601,233	2,390,924
Less investment expenses:		
Securities lending borrower rebates	(1,544,051)	(1,649,503)
Custody fees	(479,286)	(341,194)
Investment services	<u>(20,418,398)</u>	<u>(11,557,450)</u>
Net investment income	<u>251,859,842</u>	<u>316,607,754</u>
Contributions:		
Employer	87,373,312	83,290,516
Employee	<u>17,748,241</u>	<u>17,355,730</u>
Total contributions	105,121,553	100,646,246
Other income	<u>344,399</u>	<u>584,424</u>
Total net additions to plan net assets	<u>357,325,794</u>	<u>417,838,424</u>
Deductions from plan net assets:		
Benefit payments	111,330,798	103,393,633
Withdrawal payments and refunds of contributions	1,069,858	801,314
Administrative expenses and professional fees	<u>2,995,209</u>	<u>2,898,418</u>
Total deductions from plan net assets	<u>115,395,865</u>	<u>107,093,365</u>
Net increase in plan net assets	241,929,929	310,745,059
Plan net assets held in trust for pension benefits:		
Beginning of year	<u>2,493,803,928</u>	<u>2,183,058,869</u>
End of year	<u>\$ 2,735,733,857</u>	<u>2,493,803,928</u>

See accompanying notes to basic financial statements.

DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements December 31, 2005 and 2004

1. Description of Plan and Summary of Significant Accounting Policies

General

The Dallas Police and Fire Pension System (the System) is a single-employer pension and retirement fund for police officers and firefighters employed by the City of Dallas, Texas (the City or Employer). The general terms "police officers" and "firefighters" also include fire and rescue operators, fire alarm operators, fire inspectors, apprentice police officers, and apprentice firefighters. The System is comprised of a single defined benefit pension plan, called the "Combined Pension Plan," designed to provide retirement, death, and disability benefits for firefighters and police officers (members). The System was originally established under former Article 6243a of the Revised Civil Statutes of Texas, and since 1989, derives its authority to continue in operation under the provisions of Article 6243a-1 of the Revised Civil Statutes of Texas. All active police officers and firefighters (as defined above) employed by the City are required to participate. As of December 31, 2005 and 2004, the System's membership consisted of:

	<u>2005</u>	<u>2004</u>
Nonactive member:		
Pensioners and qualified survivors currently receiving benefits and terminated employees entitled to benefits but not yet receiving them:		
Firefighters	1,369	1,338
Police officers	1,752	1,696
Terminated vested members not yet receiving benefits	<u>141</u>	<u>156</u>
Total nonactive members	<u>3,262</u>	<u>3,190</u>
Current employees:		
Vested:		
Firefighters	1,405	1,388
Police officers	<u>2,346</u>	<u>2,325</u>
Total vested current employees	<u>3,751</u>	<u>3,713</u>
Nonvested:		
Firefighters	271	291
Police officers	<u>626</u>	<u>593</u>
Total nonvested current employees	<u>897</u>	<u>884</u>
Total current employees	<u>4,648</u>	<u>4,597</u>

Continued

DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements, Continued

Pension benefits

Group A members of the Combined Pension Plan may elect to receive one of two benefit structures:

- Members with 20 years or more of pension service are entitled to normal monthly pension benefits beginning at age 50 equal to 50% of the base pay as defined as the maximum monthly civil service pay established by the City for a police officer or firefighter at the time of retirement plus 50% of the Longevity Pay the member was receiving at the time he or she left active service with the City or the effective date the member joined the Deferred Retirement Option Plan (DROP). Benefit payments are adjusted according to changes in base pay. Additionally, a member is eligible to receive 50% of the difference between any annualized City Service Incentive Pay granted to the member less annual Longevity Pay. Members who meet the service prerequisite may elect to take early retirement at age 45 with reduced pension benefits.
- Members with 20 years or more of pension service are entitled to normal monthly pension benefits beginning at age 55 equal to 3% of the base pay computed as noted in the prior paragraph for each year with a maximum of 32 years. In addition, a member receives 50% of the Longevity Pay and 1/24 of any City Service Incentive Pay the member was receiving at the time he or she left active service with the City or the effective date the member joined DROP. Pension benefit payments are increased in the same manner as under Group B (described below). Members who meet the service prerequisite may elect to take early retirement at age 50 with reduced pension benefits.

Group B Benefit - Members with five or more years of pension service are entitled to monthly pension benefits beginning at age 50 equal to 3% of the member's average Computation Pay determined over the highest 36 consecutive months of Computation Pay, multiplied by the number of years of pension service, up to a maximum of 32 years. Computation Pay, for purposes of this calculation, includes Civil Service pay for the highest rank attained by competitive exam and any educational incentive, longevity or City Service Incentive Pay. Certain members who meet the service prerequisite may elect to take early retirement with reduced benefits starting at age 45. A Group B member who has accrued 20 or more years of Pension Service and who has been on Active Service at any time on or after January 1, 1999 may take a pension benefit regardless of age. The pension benefit calculation would be the same except the percent multiplier would be based on the member's age at the time of applying for the pension. In addition, Group B benefits are increased by 4% of the initial benefit amount each October 1.

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DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements, Continued

Additional benefits available under the System:

- Members with over 20 years of pension service, upon attaining age 55, shall receive a monthly supplement equal to the greater of \$75 or 3% of their total monthly benefits (excluding the benefit supplement amount).
- Disability benefits are available for members who become disabled during the performance of their duties from the first day of employment. Reduced disability benefits are also available for nonduty-related disabilities as are survivor benefits for qualified survivors.
- Members who are eligible to retire are allowed to enter the DROP program. DROP members have their contribution discontinued but the City's portion of the total contribution continues. The member's monthly benefit remains in the System in a DROP Account and accumulates interest. Upon retirement from the City, the Member is able to withdraw from their DROP Account along with the normal benefits. DROP members' balances are \$428,990,153 and \$358,726,070 for December 31, 2005 and 2004, respectively.
- A minimum benefit is paid to vested retired members of an amount not less than \$2,200 per month subject to any restrictions contained in the Plan document. The minimum benefit is prorated for members who retire with less than 20 years of service credit and \$1,200 monthly for Qualified Surviving Spouse, if there are no Qualified Surviving Children receiving benefits. The minimum benefit is \$1,100 monthly for Qualified Surviving Children and Qualified Surviving Spouse if qualified surviving children are receiving benefits.

Contributions

As a condition of participation, Group A members are required to contribute to the System 6.5% of their base pay, as defined in the System's plan document. Group B members are required to contribute to the System 8.5% of their Computation Pay, as defined in the System's plan document. Article 6243a-1 of the Revised Civil Statutes of Texas requires the City to make contributions of 27.5% of total wages and salaries as defined in the System's plan document, in accordance with schedules contained in the plan document.

The contribution schedules contained in the plan document can be changed by the Texas State Legislature or majority votes of the voters of the City.

Members of Group B are immediately vested in their member contributions and, with five years of pension service may, at termination of employment, leave their contribution on deposit with the System and receive a monthly benefit at normal retirement age. If a member's employment is terminated and is not eligible for a future benefit or the member elects not to receive present or future pension benefits, the member's contributions to the System are returned, without interest, upon written application. If application for refund is not made within three years, the member who is not eligible for a future benefit forfeits the right to a refund of his or her contribution; however, a procedure does exist whereby the member's right to the contributions can be reinstated. Under current law, Group A members must have 20 years of service to be eligible for a benefit. Group A member contributions are not refunded upon termination from employment.

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DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements, Continued

Termination

Although the System has not expressed any intent to do so, in the event the System is terminated or upon complete discontinuance of contributions, the members and their beneficiaries shall be entitled to the benefits accrued to the date of such termination or discontinuance, to the extent then funded.

System administration

The System is administered by a twelve-member Board of Trustees (the Board) consisting of four City Council members appointed by the City Council, three police officers and three firefighters, all elected by employees of their respective departments, who are members of the System, and one pensioner who has retired from the Police Department and one pensioner who has retired from the Fire Department and each are elected by pensioners from their respective departments.

Basis of presentation

The accompanying basic financial statements are presented in accordance with generally accepted accounting principles established by the Governmental Accounting Standards Board (GASB), which designates accounting principles and financial reporting standards applicable to State and local governmental units. The accompanying basic financial statements include solely the accounts of the System, which include all programs, activities and functions relating to the accumulation and investment of the net assets and related income necessary to provide the service, disability and death benefits required under the terms of the governing statutes and amendments thereto.

Adoption of new accounting pronouncement

The GASB has issued Statement No. 40, *Deposit and Investment Risk Disclosures*, which amends GASB Statement No. 3, *Deposits with Financial Institutions, Investments (Including Repurchase Agreements), and Reverse Repurchase Agreements*. GASB Statement No. 40 requires disclosure information related to common risks inherent in deposit and investment transactions. The statement is effective for financial statements beginning after June 15, 2004 and accordingly, has been implemented by the System in fiscal year 2005.

Recent accounting pronouncement

The GASB has issued Statement No. 44, *Economic Condition Reporting*, which amends National Council on Governmental Accounting Statement No. 1, *Governmental Accounting and Financials Reporting Principles* that guide the preparation of the statistical section. GASB Statement No. 44 requires disclosure information related to statistical data to assess the economic condition of a government. The statement is effective for financial statements for periods beginning after June 15, 2005 and accordingly, will be implemented by the System in fiscal year 2006.

Reclassifications

Certain amounts in 2004 have been reclassified to conform to current year presentation.

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DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements, Continued

Basis of accounting

The basis of accounting is the method by which revenues and expenses are recognized in the accounts and reported in the basic financial statements. The accrual basis of accounting is used by the System. Under the accrual basis of accounting, revenues, which include contributions and investment income, are recognized when they are earned and collection is reasonably assured, and expenses are recognized when the liability is incurred. Member and Employer contributions are recognized as revenue in the period in which the compensation is earned. In addition, the System records contributions according to System requirements and State statute. Benefits paid to members and contribution refunds are recognized when due and payable in accordance with the terms of the System. Accrued income, when deemed uncollectible, is charged to operations.

Accordingly, interest earned but not received and dividends declared but not received as of the System's fiscal year-end are recorded as accrued interest and dividends receivable, respectively. In addition, unsettled investment purchases and sales are accrued.

Reporting entity

The System is a component unit of the City and its basic financial statements and required supplemental information are included in the City's Comprehensive Annual Financial Report.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the basic financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and cash equivalents

The System considers only demand deposits as cash. Cash equivalent securities, which are composed of all highly liquid investments with a maturity of three months or less when purchased, are considered to be cash equivalents.

Investment valuation and income recognition

Statutes of the State of Texas authorize the System to invest surplus funds in the manner provided by the Government Code, Title 8, Subtitle A, Subchapter C. This subchapter provides for the investment of surplus assets in any investment or investments that are deemed "prudent" by the Board. The investment policy of the Board does not restrict the types of investments authorized to be made on behalf of the System. The investment policy is based upon an asset allocation study that considers the current and expected condition of the System, the expected long-term capital market outlook and the System's risk tolerance.

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DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements, Continued

Investments are reported at fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Short-term investments are government and corporate bonds with a maturity of less than one year and are valued based on current market rates. The fair value of limited partnerships, real estate trusts, and real estate loans is based on independent appraisals and recent financial results. Investments that do not have an established market are reported at their estimated fair values.

Unrealized gains and losses are presented as net appreciation in fair value of investments on the statement of changes in plan net assets along with gains and losses realized on sales of investments. Purchases and sales of investments and forward foreign exchange contracts are recorded on the trade date. Gains or losses on forward foreign exchange contracts are recognized when the contract is complete.

Dividend income is recorded on the ex-dividend date. Interest and income from other investments are recorded as earned.

Benefits

Benefits and refunds of contributions are recorded in these basic financial statements when they are paid to participants.

Foreign currency transactions

The System is a party to certain financial arrangements, utilizing forward contracts, options and futures only as a hedge against foreign currency fluctuations. Entering into these arrangements involves not only the risk of dealing with counterparties and their ability to meet the terms of the contracts but also the risk associated with market fluctuations. Gains and losses on option and future arrangements are recorded as they are incurred. Gains and losses on forward contracts are recorded on the settlement date.

Gains and losses resulting from foreign exchange contracts (transactions denominated in a currency other than the System's functional currency - United States dollars) are recorded by the System based on changes in market values and are combined with similar transactions in the accompanying statements of changes in plan net assets and are included in net investment income. The System structures its foreign exchange contracts and enters into certain transactions to substantially mitigate the System's exposure to fluctuations in foreign exchange rates.

Investments and broker accounts denominated in foreign currencies outstanding at December 31, 2005 and 2004 were converted to the System's functional currency (United States dollars) at the foreign exchange rates quoted at December 31, 2005 and 2004. These foreign exchange gains and losses are included in net appreciation in fair value of investments in the accompanying statements of changes in plan net assets.

Administrative expenses

The cost of administering the System is paid by the System from current earnings pursuant to an annual fiscal budget adjusted by the Board.

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DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements, Continued

2. Cash and Cash Equivalents

For cash deposits and cash equivalents, custodial credit risk is the risk that in the event of a bank failure, the System's deposits may not be returned to it. The System's deposits are held by the Custodian, JP Morgan. As of December 31, 2005 and 2004, the System had bank balances of \$1,046,554 and \$0, respectively, that are in demand deposit accounts subject to coverage by Federal deposit insurance, but not collateralized. The System does not have a deposit policy for custodial credit risk; however, the System's credit risk exposure is mitigated by the financial strength of the banking institution in which the deposits are held.

3. Investments

Portions of the System's investments are classified as security investments. A security is a transferable financial instrument that evidences ownership or creditorship. Investments in commingled funds, limited partnerships, real estate trusts, and loans and mortgages are investments that are evidenced by contracts rather than securities.

The fair values of the System's investments at December 31, 2005 and 2004 are presented by type, as follows:

	<u>2005</u>	<u>2004</u>
Cash and short term investments	\$ 272,737,505	288,678,041
United States government securities	21,086,315	20,234,022
U.S. government sponsored enterprises	34,239,013	8,700,000
Foreign government securities	247,540,762	193,837,110
Commingled funds	89,005,318	373,501,808
Domestic equities	831,471,786	501,582,329
International equities	660,850,977	598,469,171
Corporate securities	373,824,612	306,908,250
Investments, at appraised value - real estate equity funds	<u>546,201,086</u>	<u>383,872,834</u>
Total investments	\$ <u>3,076,957,374</u>	<u>2,675,783,565</u>

The Board has contracted with investment managers to manage the investment portfolio of the System, subject to the policies and guidelines established by the Board. The Board has custody agreements with JP Morgan Chase and under such agreements JP Morgan Chase assumes responsibility for the safekeeping of certain investments, handling of transactions based on the instructions of investment managers, and accounting for the investment transactions.

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DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements, Continued

Investments that individually represent 5% or more of the net assets available for benefits and the total of investments that individually represent less than 5% of the net assets available for benefits at December 31 are as follows:

	2005		2004	
	Number of shares/units	Fair value	Number of shares/units	Fair value
Investments greater than 5% of net assets, at quoted market value:				
Bank commingled trust funds -				
S&P 500 Index fund State Street Global Advisors			1,622,502	358,491,872
Securities lending -				
Global Securities Lending JP Morgan		<u>207,815,275</u>		<u>164,927,817</u>
Total investments greater than 5% of net assets		207,815,275		523,419,689
Investments less than 5% of net assets:				
At quoted market value		2,322,941,014		1,768,491,042
At appraised value		<u>546,201,085</u>		<u>383,872,834</u>
Total investments		<u>3,076,957,374</u>		<u>2,675,783,565</u>

Custodial credit risk

For an investment, custodial credit is the risk that, in the event of the failure of the counterparty, the System will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the System, and are held by either the counterparty or the counterparty's trust department or agent but not in the System's name. At December 31, 2005, the System's security investments that were not subject to custodial credit risk were the investments in fixed income and equity investments.

Concentration of credit risk

The allocation of assets among various asset classes are set by the Board with the objective of optimizing the investment return of the System within framework of acceptable risk and diversification. For major asset classes (e.g., domestic equities, international equities, fixed income, alternative investments, and real estate), the System will further diversify by employing investment managers who implement the strategies selected by the Board.

Continued

DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements, Continued

Significant guidelines are as follows:

Public market investments

1. Specific guidelines are developed cooperatively by the System's investment staff, legal counsel, and investment manager and shall be incorporated into the Investment Management Services Contract executed by the Chair of the Board, System Administrator, General Counsel, and the investment manager.
2. In case of conflict between the specific manager guidelines and the general guidelines, the specific guidelines, as approved by the Board, shall supersede. The general guidelines are as follows:
 - a. Manager investment philosophy, style, and strategy shall remain consistent and shall not change without the Board's approval. The manager shall have discretion to manage the portfolio consistent with the style presented to the Board at the time of selection and further subject to the restrictions established by the policy herein.
 - b. The following transactions are prohibited: short sales, selling on margin, put and call options, and the use of derivatives for speculation unless authorized by the Board.
 - c. Transactions that involve a broker acting as a principal, where such broker is also affiliated with the manager who is making the transaction are prohibited, unless specifically approved by the Board.
 - d. Transactions shall be executed at competitive costs, or within the parameters established for directed brokerage transactions by the Board.
 - e. Managers shall maintain cash levels consistent with their style as presented to the Board at the time of selection. Any deviation shall be allowed only after notifying the System Administrator and Assistant Administrator of Investments and should be related to unusual market conditions. The cash level held by each manager will be addressed in the Investment Management Services Contract.
3. The Board with the assistance from the System staff shall monitor each investment manager's performance and adherence to style, strategy, and manager specific guidelines. It is the Board's discretion to take corrective action by replacing an investment manager if they deem it appropriate at any time.

Alternative and real estate investments

1. The investment specific guidelines for each manager will be incorporated in a Limited Partnership Agreement, Limited Liability Company Agreement, or other binding agreement as is appropriate for the investment. The Board, System Administrator, General Counsel, and the investment manager execute this document.
2. In case of conflict between the specific manager guidelines and the general guidelines, the specific guidelines, as approved by the Board, shall supersede. The general guidelines are as follows:

Continued

DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements, Continued

- a. Manager investment philosophy, style, and strategy shall remain consistent and shall not change without the Board's approval. The manager shall have discretion to manage the portfolio consistent with the style presented to the Board at the time of selection and further subject to the restrictions established by the policy herein.
 - b. The Chair of the Board may execute amendments and consents if the resulting changes or allowances are provided for in the governing documents as previously accepted by the Board. Otherwise, such changes are to be approved by the Board. The Board will be notified on a quarterly basis of all executed amendments.
3. The Board with assistance from the System staff shall monitor each Alternative and Real Estate manager's performance and adherence to strategy and manager specific guidelines. It is the Board's discretion to take corrective action by replacing an investment manager if they deem it feasible and appropriate at any time. Alternative and Real Estate investment manager retention is governed in most cases by Limited Partnership Agreements, Limited Liability Company Agreements, or other binding agreements. In these cases, the Board with assistance from the System staff shall identify available options as allowed by the governing documents and determine the impact and consequences of these options.

Interest rate risk and foreign currency risk

The System invests in fixed income securities including, but not limited to, investments representing instruments with an obligated fixed rate of interest including public and private debentures, mortgages, investments in life insurance general accounts and guaranteed investment contracts, with maturities greater than one year, and options/futures. Instruments may have an investment grade or non-investment grade rating. Purchases and sales, investment selection and implementation of investment strategies are delegated to the discretion of the investment manager, subject to compliance with its management agreement and the System's Investment Policy.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of the investment. Interest rate risk is the greatest risk faced by an investor in the fixed income market. The price of a fixed income security typically moves in the opposite direction of the change in interest rates. The weighted average maturity expresses investment time horizons (when the investment come due and payable) in years, weighted to reflect the dollar size of individual investments within the investment type. The System does not have a formal investment policy that limits investment maturities as a means of managing its exposure to potential fair value losses arising from future changes in interest rates, but rather mandates such limits within the Investment Management Services Contract.

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. International securities investment managers are expected to maintain diversified portfolios by sector and by issuer using the System Investment Policy.

At December 31, 2005, the following tables shows the System's investments by type, time-to-maturity, fair value, and foreign currency fluctuation:

Continued

DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements, Continued

The following tables provide information as of December 31, 2005, concerning the fair value of investments, interest rate risk, and foreign currency risk:

Type of Investment	Less Than 1 Year	1-5 Years	6-10 Years	More Than 10 Years	Total Fair Value
Fixed Maturity Domestic:					
U.S. Treasury Securities	\$ 19,317,194	469,241	906,732	393,148	21,086,315
U.S. Gov't Agency Securities	44,941	32,150,978		2,043,094	34,239,013
Corporate Securities:					
Asset Backed Securities		118,302	2,424,550	6,045,916	8,588,768
Collateralized Mortgage Obligation	19,496		118,407	8,874,817	9,012,720
Corporate Bonds	2,215,665	32,711,370	89,545,534	65,539,778	190,012,347
Comingled Funds				89,005,318	89,005,318
Convertible Bonds	2,123,438	7,711,956	2,454,675	14,161,949	26,452,018
Investment interests				102,713,001	102,713,001
Total fixed maturity domestic	<u>23,720,734</u>	<u>73,161,847</u>	<u>95,449,898</u>	<u>288,777,021</u>	<u>481,109,500</u>
International Government Bonds:					
Australian Dollar		9,688,976	5,244,119		14,933,095
Argentina		2,020,064		317,737	2,337,801
Brazil Real				5,302,193	5,302,193
British Pound Sterling		369,860	5,560,867		5,930,727
Canadian Dollar	12,899,965		8,778,442		21,678,407
EURO Currency	1,451,572	29,287,026	9,453,652	8,831,283	49,023,533
Japanese Yen	6,375,540	20,354,028	9,576,516		36,306,084
Mexican New Peso			6,976,809	801,634	7,778,443
New Zealand Dollar			3,070,590		3,070,590
Poland		9,609,891			9,609,891
Peru				1,378,125	1,378,125
Singapore Dollar		7,742,254			7,742,254
South African Rand	2,387,835				2,387,835
Swedish Krona		3,992,285	11,206,456		15,198,741
Uruguay			1,898,820	1,560,239	3,459,059
Total international government bonds	<u>23,114,912</u>	<u>83,064,384</u>	<u>61,766,271</u>	<u>18,191,211</u>	<u>186,136,778</u>
International Corporate Bonds:					
Australian Dollar	1,060,614		1,077,638		2,138,252
Bermuda			102,715	109,206	211,921
British Pound Sterling	1,376,712	3,091,618	7,114,903	1,105,130	12,688,363
Cayman Islands	2,104,167			2,244,937	4,349,104
Chile				39,819	39,819
Canadian Dollar	1,123,665	744,574	3,185,925	1,766,033	6,820,197
EURO Currency	213,721	861,652	4,315,263	1,354,257	6,744,893
Japanese Yen				99,626	99,626
Mexican New Peso	68,733			15,037	83,770
Philippines				2,120,550	2,120,550
Singapore Dollar		400,363			400,363
Venezuela				1,348,900	1,348,900
Total international corporate bonds	<u>5,947,612</u>	<u>5,098,207</u>	<u>15,796,444</u>	<u>10,203,495</u>	<u>37,045,758</u>
Pooled International Fixed Maturity		<u>1,572,373</u>		<u>59,831,611</u>	<u>61,403,984</u>
Total international fixed maturity	<u>29,062,524</u>	<u>89,734,964</u>	<u>77,562,715</u>	<u>88,226,317</u>	<u>284,586,520</u>
Total fixed maturity	<u>\$ 52,783,258</u>	<u>162,896,811</u>	<u>173,012,613</u>	<u>377,003,338</u>	<u>765,696,020</u>

Continued

DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements, Continued

Credit risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Fund does not have a formal policy limiting investment credit risk, but rather mandates such limits within the Investment Management Services Contract. The Fund's exposure to investment credit risk in fixed income securities as of December 31, 2005 is as follows:

Type	Moody Rating	Amount	Percentage of Holdings	Type	Moody Rating	Amount	Percentage of Holdings
Corporate securities:				Mortgage bonds			
Asset backed securities							
Aaa		\$ 1,038,482	0.14%	A2		29,327	0.00%
Aaae		55,236	0.01%	Aa1		26,836	0.00%
B2		275,157	0.04%	Aa2		24,783	0.00%
Ba2		758,597	0.10%	Aa2e		18,112	0.00%
Baa2		129,044	0.02%	Aaa		3,208,236	0.42%
Baa3		1,233,418	0.16%	Aaae		49,136	0.01%
NR		3,994	0.00%	Ba1		50,920	0.01%
WR		<u>5,094,840</u>	<u>0.67%</u>	Ba2		535,827	0.07%
Total asset backed securities		<u>8,588,768</u>	<u>1.14%</u>	Baa2		19,496	0.00%
Convertible bonds				Baa3		401,257	0.05%
B3		2,708,493	0.35%	NR		3,264,306	0.43%
Ba2		5,875,330	0.77%	WR		<u>1,384,484</u>	<u>0.18%</u>
C		664,538	0.09%	Total mortgage bonds		<u>9,012,720</u>	<u>1.17%</u>
Ca		445,031	0.06%	Investment fund	NR	<u>102,713,001</u>	<u>13.41%</u>
Caa1		3,373,000	0.44%	Total corporate securities		<u>373,824,612</u>	<u>48.84%</u>
Caa2		709,813	0.09%	Government sponsored enterprises			
Caa3		2,288,638	0.30%	Aaa		34,137,797	4.46%
NR		10,154,675	1.33%	P-1		<u>101,216</u>	<u>0.01%</u>
WR		<u>232,500</u>	<u>0.03%</u>	Total government sponsored enterprises		<u>34,239,013</u>	<u>4.47%</u>
Total convertible bonds		<u>26,452,018</u>	<u>3.46%</u>	Foreign government securities:			
Corporate bonds				Government bonds			
A1		2,456,943	0.32%	A2		48,100,046	6.28%
A2		2,850,719	0.37%	Aa2		1,812,546	0.24%
A2e		126,189	0.02%	Aaa		82,545,297	10.78%
A3		3,760,629	0.49%	B3		6,850,800	0.89%
A3e		59,072	0.01%	Ba3		6,680,318	0.87%
Aa1		4,741,178	0.62%	Baa1		10,166,278	1.33%
Aa1e		2,929,968	0.38%	NR		<u>78,485,512</u>	<u>10.25%</u>
Aa2		4,142,825	0.54%	Total government bond		<u>234,640,797</u>	<u>30.64%</u>
Aa3		3,014,033	0.39%	Treasury bill			
Aaa		3,901,712	0.51%	NR		<u>12,899,965</u>	<u>1.68%</u>
B1		23,364,474	3.05%	Total foreign government		<u>247,540,762</u>	<u>32.32%</u>
B2		28,421,808	3.71%	Unites States government securities			
B3		28,922,357	3.78%	Treasury Bill	P-1	17,713,901	2.31%
Ba1		5,822,187	0.76%	Treasury Bond	Aaa	636,590	0.08%
Ba2		21,042,994	2.75%	Treasury Note	Aaa	<u>2,735,824</u>	<u>0.36%</u>
Ba3		19,586,125	2.56%	Total U.S. government securities		<u>21,086,315</u>	<u>2.75%</u>
Baa1		3,929,795	0.51%	Commingled			
Baa1e		40,118	0.01%	NR		<u>89,005,318</u>	<u>11.62%</u>
Baa2		6,334,600	0.83%	Total credit risk debt securities		<u>\$ 765,696,020</u>	<u>100.00%</u>
Baa2e		40,158	0.01%				
Baa3		11,907,597	1.56%				
Ca		262,398	0.03%				
Caa1		14,805,275	1.93%				
Caa2		1,195,200	0.16%				
Caa3		1,169,356	0.15%				
NR		11,483,009	1.50%				
WR		<u>20,747,386</u>	<u>2.71%</u>				
Total corporate bonds		<u>227,058,105</u>	<u>29.66%</u>				

Continued

DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements, Continued

4. **Securities Lending**

The Board has authorized the System to enter into an agreement with JP Morgan Chase (JP Morgan) for the lending of certain of the System's securities (the Securities Lending Program or program) including, but not limited to, stocks and bonds to counterparty brokers and banks (borrowers), for a predetermined period of time and fee. Such transactions are allowed by State statute.

During 2005 and 2004, JP Morgan lent, on behalf of the System, securities held by JP Morgan as the System's custodians, and received United States dollar cash and United States Government securities as collateral. JP Morgan did not have the ability to pledge or sell collateral securities absent a borrower default. Borrowers were required to put up collateral for each loan equal to: (i) in the case of loaned securities denominated in United States dollars or whose primary trading market was in the United States or sovereign debt issued by foreign governments, 102% of the fair market value of the loaned securities; and (ii) in the case of loaned securities not denominated in United States dollars or whose primary trading market was not in the United States, 105% of the fair market value of the loaned securities.

The Board did not impose any restrictions during 2005 and 2004 on the amount of the loans that JP Morgan made on its behalf. There were no failures by any borrowers to return the loaned securities or pay distributions thereon during the fiscal years 2005 and 2004. Moreover, there were no losses during the 2005 and 2004 fiscal years resulting from a default of the borrower, JP Morgan. JP Morgan maintains a Banker's Blanket Bond in the amount of \$75 million and has insurance coverage in the amount of \$50 million for any losses which could result from borrower's defaults.

During 2005 and 2004, the Board and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral was invested, together with the collateral of other qualified tax-exempt plan lenders, in a collective investment pool maintained by JP Morgan. The relationship between the average maturities of the investment pool and the Board's loans was affected by the maturities of the loans made by other plan entities that invested cash collateral in the collective investment pool, which the Board could not determine. On December 31, 2005 and 2004, the System had no credit risk exposure to borrowers. The market value of securities on loan and collateral held for the System were \$201,882,969 and \$207,815,275 at December 31, 2005, and \$161,013,456 and \$164,927,817 at December 31, 2004.

Disclosure of securities lending revenue is shown gross with the associated reductions for investment expenses on the face of the statements of changes in plan net assets, and the cash collateral and associated securities lending payable is shown on the face of the statements of plan net assets for December 31, 2005 and 2004.

5. **Contributions Required and Contributions Made**

Funding policy

Contribution rates are established to remain level over time as a percentage of members' salaries. The contribution rate has been determined to provide for normal cost plus the level percentage of members' salaries required to amortize the unfunded actuarial accrued liability (or surplus) over 20 years as of January 1, 2006 compared to 29 years as of January 1, 2005.

Continued

DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements, Continued

The required contribution rate of the City, pursuant to an actuarial study effective January 1, 2006, consists of 15.84% of covered members' salaries to pay normal costs, increased by 7.78% of covered members' salaries to amortize its funding deficit over 20 years, increased by 3.88% of covered members' salaries for an additional amortization requirement resulting in a net contribution rate of 27.5%. The City is required to contribute at a rate that has been actuarially determined and adopted by the Board.

In 2005 and 2004, combined police officers, firefighters and City contributions represent approximately 27.5% and 35.75%, respectively of each year's covered payroll. State law requires that the System fund the plan benefits based on an approved actuarial study. The actuary must certify that the contribution commitment by police officers, firefighters and the City provides an adequate financing arrangement. During 2005 and 2004, contributions were made in accordance with the adopted plans of benefits approved by the System's actuary.

Historical trend information

Historical trend information is provided as supplemental information on pages 24 through 26. This information is intended to demonstrate progress the System has made in accumulating sufficient assets to pay benefits when due and the related actuarial assumptions used in determining the actuarially determined amounts.

The System's contribution rates and the actuarial information included in schedules 1 and 2 is based on certain assumptions pertaining to interest rates, inflation rates and participant demographics, all of which are subject to change. Due to uncertainties inherent in the estimations and assumptions process, it is at least reasonably possible that changes in these estimates and assumptions in the near term could be material to the financial statements.

6. Forward Contracts

During fiscal years 2005 and 2004, the System entered into forward foreign exchange contracts. A currency forward is a contractual agreement between two parties to pay or receive specific amounts of foreign currency at a future date in exchange for another currency at an agreed upon exchange rate. Forward commitments are not standardized and carry credit risk due to the possible nonperformance by one of the counterparties. The maximum potential loss is the aggregate face value in U.S. dollars at the time the contract was opened; however, the likelihood of such loss is remote. Forwards are usually traded over-the-counter. These transactions are entered into in order to hedge risks from exposure to foreign currency rate fluctuation and to facilitate trade settlement of foreign security transactions. Forwards carry market risk resulting from adverse fluctuations in foreign exchange rates. Recognition of realized gain or loss depends on whether the currency exchange rate has moved favorable or unfavorable to the contract holder upon termination of the contract. Prior to termination of the contract, the System records the unrealized currency translation gain or loss based on the applicable forward exchange rates. Such matching existed at year end.

During 2005 and 2004, the System recognized net realized losses on foreign currency forward contracts of \$305,327 and \$1,199,639, respectively. At December 31, 2005 and 2004, the System had net unrealized depreciation on forward contracts reflected in the accompanying basic financial statements of approximately \$1,714,801 and \$8,179, respectively.

Continued

DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements, Continued

7. **Obligation Under Reverse Repurchase Agreements**

State statutes permit the System to enter into reverse repurchase agreements. The credit exposure at year end 2005 related to these agreements was \$2,369,792. All sales of investments under reverse repurchase agreements are for fixed terms. In investing the proceeds of reverse repurchase agreements, the System policy is for the term to maturity of the investment to be the same as the term of the reverse repurchase agreements. Such matching existed at year end 2005 and 2004.

8. **Line of Credit**

The System has a credit agreement with a commercial bank which provides for a revolving line of credit bearing interest of 4.7% at December 31, 2005, payable monthly. At December 31, 2005, the System had borrowed approximately \$86,391,000 related to the revolving credit line which provides for a maximum borrowing of \$100,000,000. The revolving credit line was opened in July 2005, and expires on July 6, 2006. Interest rate is based on LIBOR plus 40 basis points. The System also pays a quarterly fee on the unused portion of the line of credit.

9. **Federal Income Tax Status**

A favorable determination that the System is qualified and exempt from Federal income taxes was received on January 24, 2001, from the Internal Revenue Service (IRS). The Board believes that the System is designed and continues to operate in compliance with the applicable requirements of the Internal Revenue Code.

10. **Administrative Expenses**

The System's plan document authorizes the Board to pay administrative costs from the System, provided that the System's actuary has determined that the System has sufficient income to pay such costs. Of the System's total administrative costs, \$418,863 and \$546,426 were reimbursed to the City by the System during the years ended December 31, 2005 and 2004, respectively.

Investment related expenses for the years ended December 31, 2005 and 2004 also include \$13,552,627 and \$10,685,754, respectively, in asset management fees.

11. **Commitments and Contingencies**

As described in note 1, certain members of the System are entitled to refunds of their accumulated contributions on termination of employment with the City, prior to being eligible for pension benefits. As of December 31, 2005 and 2004, aggregate contributions from active members of the System with less than five years of service were \$4,597,367 and \$7,056,275, respectively,

The System had outstanding investment commitments to various limited partnerships and international investment advisors of approximately \$288 million at December 31, 2005.

Continued

DALLAS POLICE AND FIRE PENSION SYSTEM

Notes to Basic Financial Statements, Continued

12. Deferred Compensation Plans

The System offers its employees a deferred compensation plan (the DCP) created in accordance with Internal Revenue Code Section 457. The DCP, available to all employees of the System, permits employees to defer a portion of their salary until future years. Distributions from the DCP are not available to employees until termination, retirement, death or unforeseeable emergency. The DCP has a third party administrator, ING Retirement Services (ING) and the cost of administration and funding are borne by the DCP participants. Amounts deferred are held in trust by ING and since the System had no fiduciary responsibility for the DCP, these amounts are not reflected in the accompanying basic financial statements in accordance with GASB Statement No. 32.

The System also offers its employees a money purchase pension plan (MPP) created in accordance with Internal Revenue code Section 401. The plan is available to employees of the System that are not considered an employee of the City. Participation in the plan is with the performance of one hour of service and termination from the plan is upon employment termination. Employees are allowed to make after tax contributions, not to exceed IRS Code limitations. System contributions equal a percentage of the employee's compensation that is equal to the contributed amount the City makes on behalf of a System participant. During 2005 and 2004, the System contributed \$139,680 and \$179,713, respectively. The MPP has a third party administrator, ING, Inc., and the cost of administration and funding are borne by the MPP participants. Amounts deferred are held in trust by ING and since the System had no fiduciary responsibility for the MPP, these amounts are not reflected in the accompanying financial statements in accordance with GASB Statement No. 32.

13. Risks and Uncertainties

The System invests in various investments securities. Investment securities are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the value of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the statements of plan net assets.

The System contribution rates and the actuarial information included in the schedule of contributions, page 25, and schedule of funding progress, page 24, are based on certain assumptions pertaining to interest rates, inflation rates and participant demographics, all of which are subject to change. Due to uncertainties inherent in the estimations and assumptions process, it is at least reasonably possible that changes in these estimates and assumptions in the near term could be material to the basic financial statements.

Several lawsuits are pending against the City by third party police officers and firefighters, which claim the right to significant back pay on behalf of most current and many former Dallas police officers and firefighters. If these lawsuits are successful, they will likely result in large over-due pension claims on behalf of many retired pensioners and large increases in the actuarial accrued liabilities of current members of the System, because pensions are generally a percentage of the pay of the police officers and firefighters.

The System has intervened in the above lawsuits to protect the System's right to members and City contributions which the System believes will be due if the police officers' and firefighters' claims are successful. The ultimate outcome of these lawsuits cannot be determined at this time and, accordingly, no amounts related to these claims have been accrued in the Plan's basic financial statements as of December 31, 2005 and 2004.

REQUIRED SUPPLEMENTAL INFORMATION

DALLAS POLICE AND FIRE PENSION SYSTEM

Schedule of Funding Progress (Unaudited)
(dollars in millions)

GASB required supplementary information (unaudited) related to the System's funding progress is as follows (amounts are in the millions):

Schedule of Funding Progress						
Actuarial valuation date	Actuarial value of assets (a)	Actuarial accrued liability (AAL) (b)	AAL (UAAL) (b-a)	Funded ratio (a/b)	Covered payroll (c)	UAAL as a percentage of covered payroll ((b-a)/c)
1/1/1997	\$ 1,137	1,630	493	69.7%	178	277.0%
1/1/1998	1,307	1,782	475	73.3	193	246.1
1/1/1999	1,503	1,958	455	76.8	205	222.0
1/1/2000	1,772	2,094	322	84.6	213	151.2
1/1/2001	2,005	2,328	323	86.1	224	144.2
1/1/2002	2,158	2,554	396	84.5	251	157.8
1/1/2003	1,992	2,738	746	72.8	270	276.3
1/1/2004	2,286	2,889	603	79.1	265	227.5
1/1/2005	2,485	3,074	589	80.8	282	208.9
1/1/2006	2,700	3,282	582	82.3	295	197.3

Certain factors, such as changes in benefit provisions, the size or composition of the population covered by the System or the actuarial assumptions used, may significantly affect the identification of trends in the amounts reported in this schedule.

Analysis of the dollar amounts of actuarial value of assets, actuarial accrued liability, and unfunded actuarial accrued liability in isolation can be misleading. Expressing the actuarial value of assets as a percentage of the actuarial accrued liability provides one indication of the plan's funding status on a going-concern basis. Analysis of this percentage over time indicates whether the plan is becoming financially stronger or weaker, generally, the greater this percentage, the stronger the plan. Trends in unfunded actuarial accrued liability and covered payroll are both affected by inflation. Expressing the unfunded actuarial accrued liability as a percentage of covered payroll approximately adjusts for the effects of inflation and aids analysis of the plan's progress made in accumulating sufficient assets to pay benefits when due. Generally, the smaller this percentage, the stronger the plan.

See accompanying note to required supplemental schedules.

See accompanying independent auditors' report.

DALLAS POLICE AND FIRE PENSION SYSTEM

Schedule of Employer Contributions (Unaudited)
(dollars in thousands)

The following table lists required supplementary information (unaudited) related to Employer contributions (amounts in thousands):

<u>Schedule of Contributions</u>		
<u>Year ended December 31,</u>	<u>Annual required contribution</u>	<u>Percentage contributed</u>
1997	\$ 57,039	100%
1998	60,843	100%
1999	63,441	100%
2000	66,691	100%
2001	75,592	100%
2002	77,085	100%
2003	78,323	100%
2004	83,291	100%
2005	87,373	100%

The percent contributed may vary from the legally required rate as the term "Annual Required Contribution" is based upon covered payroll as of the actuarial valuation date, January 1, whereas contributions are calculated and paid based upon actual payrolls throughout the year.

Certain factors, such as changes in benefit provisions, the size or composition of the population covered by the System or the actuarial assumptions used, may significantly affect the identification of trends in the amounts reported in this schedule.

Contributions were made in accordance with actuarially determined contribution requirements as adopted by the Board of Trustees.

See accompanying note to required supplemental schedules.
See accompanying independent auditors' report.

DALLAS POLICE AND FIRE PENSION SYSTEM

Note to Required Supplemental Schedules (Unaudited)

The information presented in the required supplemental schedules was determined as part of the actuarial valuations at the dates indicated. The significant assumptions underlying the actuarial calculations at January 1, 2006 and 2005 are as follows:

Actuarially assumed investment rate of return *	8.5% per annum, compounded annually
Mortality, retirement, disability and separation rates	Graduated rates detailed in actuary's report
Projected salary increases **	Range 4.3 to 10%
Actuarial cost method	Entry age normal cost method

* Includes inflation rate of 4% and net of all expenses

** Includes inflation of 4%.

Post retirement benefit increases:	
Group A (former Plan A) and Group B members	4% of original pension annually
Group A (former Old Plan) members	4% compounded annually
Asset valuation	5-year smoothing
Amortization method	Open level percent of payroll
Remaining amortization period	20 years in 2006 and 29 years in 2005
DROP account returns	9% per annum
Post retirement mortality	1994 Group Annuity Mortality Table

The actuarial information presented was determined by the actuarial firm Buck Consultants, Inc. (formerly Mellon Consultants, Inc.) for 2005 and 2004 and results from applying various assumptions with regard to termination, disability, retirement, mortality and the time value of money to the accumulated plan benefits.

The actuarial assumptions are based on the presumption that the System will continue. Were the System to terminate, different actuarial assumptions and other factors might be applicable in determining the actuarial present value of accumulated plan benefits.

Actuarial calculations were made by the consulting actuary Buck Consultants, Inc. as of January 1, 2006 and 2005, and are not materially different from what they would have been had they been calculated on December 31, 2005 and 2004, respectively. The above assumptions are used by the System's actuaries to determine the System's obligations only, and are not used to calculate the actual System benefits. Plan benefits are fully described in the System's document.