



Comprehensive Annual Financial Report

Norfolk Employees' Retirement System

A Pension Trust Fund of the City of Norfolk, Virginia

For Fiscal Year Ended June 30, 2004

COMPREHENSIVE ANNUAL FINANCIAL REPORT

Norfolk Employees' Retirement System

A Pension Trust Fund of the City of Norfolk, Virginia

Presented by the Board of Trustees

For the Fiscal Year Ended June 30, 2004

Prepared by the Norfolk Employees' Retirement Office
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Norfolk, VA 23510
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www.norfolk.gov/Finance/Retirement

TABLE OF CONTENTS

Introductory Section

Letter of Transmittal	1
Administrative Organization	5
Organizational Chart	6

Financial Section

Independent Auditors' Report	7
Management's Discussion and Analysis	8
Financial Statements:	
Statement of Plan Net Assets	10
Statement of Changes in Plan Net Assets	11
Notes to Financial Statements	12
Required Supplementary Actuarial Information	17
Schedule of Employer Contributions	17
Actuarial Assumptions	18
Schedule of Administrative Expenses	19
Schedule of Investment Expenses	20
Schedule of Custody and Investment Consultants	20

Investment Section

Investment Performance, Policy, Statistics and Activity	21
Asset Allocation by Asset Class	22
Investment Managers and Investment Assignments	23
Target Asset Allocation	24
Investment Performance Summary	25
Schedule of Broker Commissions	26
List of Largest Assets Directly Held	27

Actuarial Section

Actuary's Certification Letter	28
Summary of Actuarial Assumptions and Methods	30
Schedule of Active Member Valuation	33
Retirees and Beneficiaries Added to and Removed from Rolls	34
Solvency Test	34
Analysis of Financial Experience	36
Summary of Plan Provisions	37
System Trends	42

Statistical Section

Active Employee Membership	44
History of Active Employee Membership	44
Retirement Granted During Fiscal Year	45
History of Retirements Granted	45
Summary of Annual Retirement Allowances	45
History of Annual Retirement Allowances	46
Income and Expenditures	46
Plan Net Assets	47
Participant and Investment Data and Ratio	47
Contribution Analysis	48

Introductory Section



City of **Norfolk**

EMPLOYEES' RETIREMENT SYSTEM

November 11, 2004

The Board of Trustees
Employees' Retirement System
City of Norfolk
Norfolk, Virginia 23510

The Comprehensive Annual Financial Report (CAFR) of the Employees' Retirement System (System) for the City of Norfolk for fiscal year ended June 30, 2004 is submitted herewith. Responsibility for both the accuracy of data, and the completeness and fairness of the presentation rests with the staff and the Board of Trustees (Board). All disclosures necessary to enable the reader to gain an understanding of the System's financial activities have been included.

As of June 30, 2004, the net assets of the system were \$816.1 million, an increase of \$65.9 million during the fiscal year. Investment return for the fiscal year was 11.2%.

The System is the administrator of a single-employer noncontributory defined benefit plan that covers substantially all employees of the City of Norfolk, excluding School Board employees who are covered by the Virginia Retirement System. Although the System presents separate financial statements, it is also included as a component unit in the City of Norfolk's CAFR.

This report consists of five sections:

1. The **Introductory Section** contains this letter of transmittal and organization chart;
2. The **Financial Section** contains the opinion of the independent auditors, the financial statements of the System and required supplementary information;
3. The **Investment Section** contains investment results and other information relating to investment policy and investment activities;
4. The **Actuarial Section** contains information from the most recent report from the System's actuary; and
5. The **Statistical Section** contains information pertaining to the membership of the System.

System History

The System was established by Section 37 of the code of the City of Norfolk, Virginia, and began operations as of January 1, 1942. Section 37 of the code as amended from time to time established the authority under which the City of Norfolk's obligation to contribute to the plan is

INTRODUCTORY SECTION

established. A single fund for all participants is used and there is no segregation of assets for individual classes of employees.

Benefit Provisions

The System provides normal and early service retirement benefits as well as death and disability benefits. All benefits vest after 5 years of creditable service effective after January 1, 1997. Ad hoc cost-of-living adjustments are provided at the discretion of the City Council. The benefit provisions of the plan are also determined by Section 37 of the code.

The Retirement Office staff provides counseling to all benefit applicants and to others requesting counseling. Presentations at new employee orientations and at various employee groups meetings are provided as requested throughout the year. All forms and retirement planning information are available in the Employees' Retirement Office, 810 Union Street, Suite 309.

Major Initiatives

During the year, the Retirement Board conducted a comprehensive review of the investment structure and investment managers. As a result of this review, the Board approved a new structure that relies on passive and enhanced indexed strategies for the core large capitalization stocks and active management of small capitalization stocks. In addition, the Retirement Board commissioned a comprehensive asset-liability study which will be completed during the coming fiscal year.

Accounting System and Internal Control

Financial statements included in this report are the responsibility of the System's management and have been prepared in accordance with the principles of governmental accounting and reporting promulgated by the Governmental Accountant Standards Board (GASB). The financial report has been prepared in accordance with GASB Statement No. 25, *Financial Reporting for Defined Benefit Plans*. The System implemented GASB Statement No. 34, *Basic Financial Statements—Managements Discussion and Analysis* as of July 1, 2001. This significant change is included in the management's discussion analysis report. These statements have been audited by Cherry, Bekaert & Holland, Certified Public Accountants & Consultants in conjunction with the City's annual audit.

The accrual basis of accounting is used to record assets and liabilities and additions and deductions of the System. Additions are recognized in the period in which they are earned, without regard to the date of collection, and deductions are recorded when the corresponding liabilities are incurred. In developing the accounting system, consideration was given to the adequacy of internal accounting controls. These were designed to provide reasonable assurance regarding the safekeeping of assets and the reliability of financial records. A continuing effort is being made toward improving the controls to assure the participants of a financially sound retirement system.

Additions and Deletions to Plan Net Assets

Employer contributions and investment income provide the funds necessary to finance retirement benefits. Employer contribution rates for fiscal years 2004 and 2003 were established in 2003 and 2002, respectively. The components of additions for the fiscal years ended June 30, 2004 and 2003 are as follows:

INTRODUCTORY SECTION

Additions and Deletions to Plan Net Assets (concluded)

	FY 2004 (thousands)	FY 2003 (thousands)	Increase (Decrease)	Percentage
Employer contributions	\$ 23,470	\$ 21,390	\$ 2,080	9.7
Investment earnings	84,898	41,341	43,557	105.4
Less investment expense	(2,102)	(1,958)	(144)	(7.4)
Total	<u>\$ 106,266</u>	<u>\$ 60,773</u>	<u>\$ 45,493</u>	74.9

The principle purpose for which the System was created is to provide retirement annuities, survivor benefits, and total and permanent disability benefits to qualified members and their beneficiaries. The cost for such programs includes recurring benefit payments as designated by the plan, refund of contributions to terminated employees, and the cost of administering the System. Deductions for fiscal year 2004 totaled \$40,062 million an increase of 5.6% over fiscal year 2003.

	FY 2004 (thousands)	FY 2003 (thousands)	Increase (Decrease)	Percentage
Benefit payments	\$ 39,592	\$ 37,416	\$ 2,176	5.8
Administrative fees	470	524	(54)	(10.3)
Total	<u>\$ 40,062</u>	<u>\$ 37,940</u>	<u>\$ 2,122</u>	5.6

Funded Status

An actuarial valuation of the System to determine funding requirements is performed annually. The actuarial valuation used for this report period was completed with payroll data as of July 1, 2003, the first day of FY 2004. Information from this report is included in the Actuarial Section.

A retirement system is fully funded when there is enough money in reserve to meet all expected future obligations to participants. As of June 30, 2004, the System's funded ratio was 90.0%.

Investments

The Board of Trustees has adopted a written Investment Policy that includes the guidelines and objectives for the investment of the System. Each investment manager must adhere to the guidelines established by the Board for investment asset quality, diversification, liquidity and risk. Both annual and longer term (3 to 10 years) goals for investment returns are established for each manager. Attainment of these goals weighs heavily in terms of whether or not a manager's contract is renewed. Typically, managers who fall below the Board's minimum objectives over the longer term are replaced.

The investment results of each manager as well as the results for the total fund are monitored by an independent investment consultant and the Chief Investment Officer who report their findings to

INTRODUCTORY SECTION

the Board on a monthly basis. In addition the System's staff produces a monthly report for the Board, detailing monthly and cumulative investment returns. The total return includes all income from dividends, interest and net gains and losses, both realized and unrealized.

In July 2003, the Board hired Summit Strategies Group as investment consultant. With assistance from the Chief Investment Officer and System staff, the Board reviews total fund and investment manager performance on at least a quarterly basis to ensure compliance with its stated objectives and policy. Staff continuously monitors performance of the System and its investment managers, and when conditions warrant, makes recommendations for change to the board.

The net assets of the System as of June 30, 2004 were \$816.1 million, an increase of \$65.9 million during the fiscal year. Investment return for the year was 11.2%. The System is financially and actuarially sound. The Retirement Fund is sound and well positioned to pay retirement benefits as they are due. A summary of the Fund's asset allocation and historic returns can be found in the Investment Section of this report.

Professional Services

Professional consultants are appointed by the Board of Trustees to perform services that are essential to the effective and efficient operation of the System. An opinion from the certified public accountant and the actuary are included in this report. The consultants appointed by the Board are listed on Page 5 of this report.

Acknowledgements

The compilation of this report reflects the combined effort of the System's staff under the leadership of the Board of Trustees. It is intended to provide complete and reliable information as a basis for making management decisions, as a means of determining compliance with legal provisions, and as a means of determining responsible stewardship of the funds of the system.

On behalf of the Board of Trustees, I would like to take this opportunity to express sincere gratitude to the staff, the advisors, and to the many people who have worked so diligently to assure the successful operation of the System.

Respectfully submitted,



Theodore O. Wilder
Executive Director

ADMINISTRATIVE ORGANIZATION

Board of Trustees

Michael S. Ives, Chair
Appointed by City Council
Term expires December 31, 2004

Robert J. Keogh, Vice Chair
Appointed by City Council
Term expires December 31, 2004

Alan Nusbaum
Appointed by City Council
Term expires December 31, 2004

Frederick V. Martin
Appointed by City Council
Term expires December 31, 2004

John D. Hopkins
Appointed by City Council
Term expires December 31, 2004

William O. Carrow, Jr.
Appointed by City Council
Term expires December 31, 2004

Regina V.K. Williams
City Manager, ex-officio

Karen R. Stephenson
Acting Director of Finance, ex-officio

Legal Advisor
Mary L. G. Nexsen
Deputy City Attorney

Custodian Bank
State Street Bank

Actuary
Mellon Human Resources & Investor
Investor Solutions

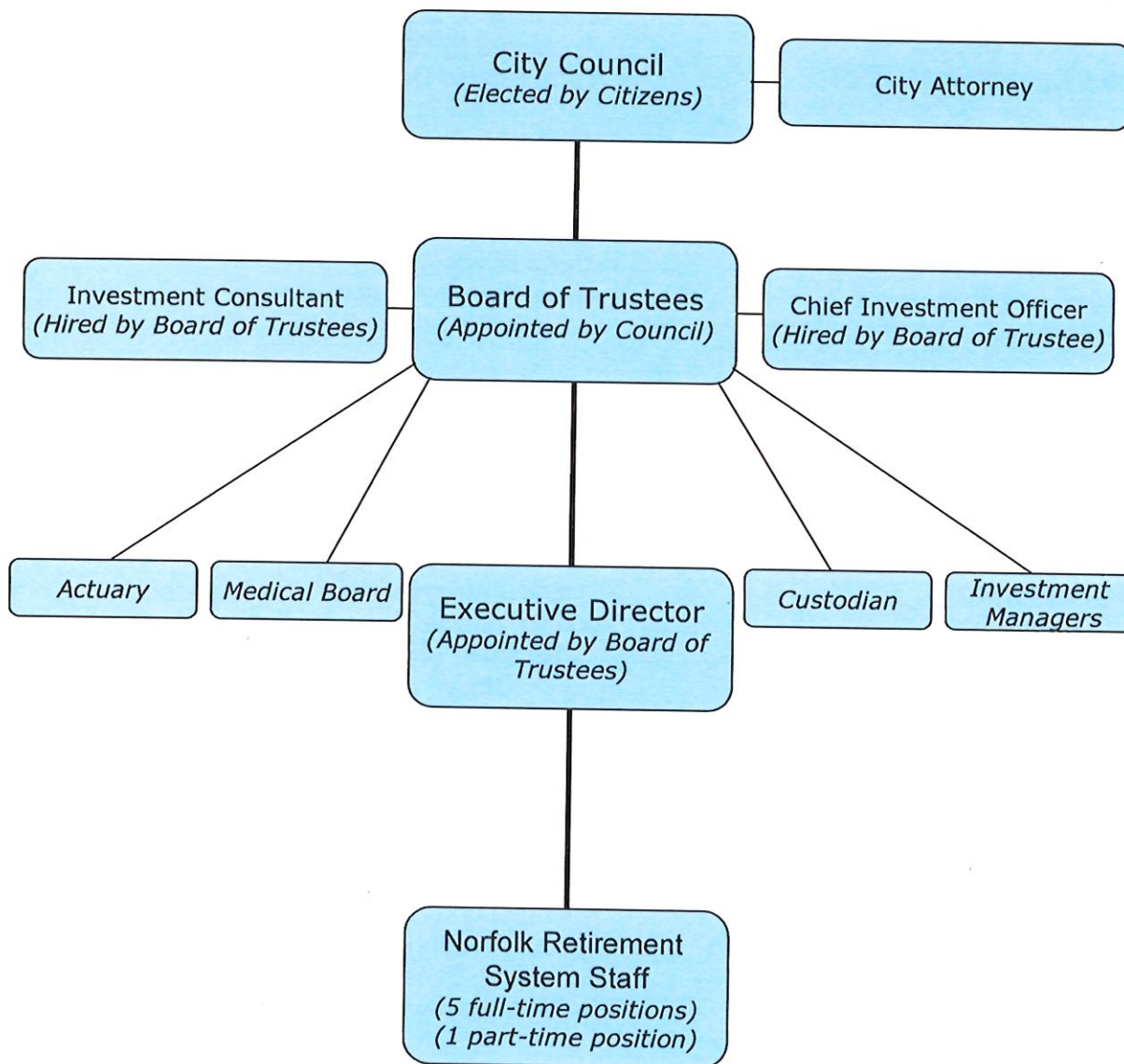
Consultants
Summit Strategies Group
Eric J. Ralph, Senior Vice President
Lotus Financial Consulting
Kamal K. Khanna, Chief Investment
Officer

Investment Managers
J. P. Morgan
Lazard Asset Management
Mellon Capital Management
Pacific Investment Management Company
Putnam Investment Management
State Street Global Advisors
Tattersall Advisory Group
Wellington Management Company
¹*Investment manager assignments can be
found on page 23.*

Employees' Retirement Administrative Staff
Theodore O. Wilder, Executive Director
Ladina M. Stevens, Assistant Executive
Director
Myrella P. Aaron, Administrative Analyst
Rhonda Lundy, Payroll Accountant
Maxine Overton, Benefits Specialist
Gail Bond, Benefits Specialist
Ravada Wesley, Benefits Specialist (part-time)

Medical Examiner
Dr. Richard L. Cullen, Jr., M.D.
Bayview Physicians Services, P.C.

ORGANIZATIONAL CHART



Financial Section



The Employees' Retirement System understands that in order to be considered for the Certificate of Achievement Award that an Independent Auditor's Report letter will have to be included in future reports. Since this report is being submitted for a general review only, the Independent Auditor's Report letter will be included when the formal Certificate of Achievement Award is applied for in fiscal year 2005.

FINANCIAL SECTION

MANAGEMENT'S DISCUSSION AND ANALYSIS

This section presents management's discussion and analysis of the System's financial performance and provides an overview of the financial activities and funding conditions for the fiscal year ended June 30, 2004.

FINANCIAL HIGHLIGHTS:

The broad United States stock market (as measured by the Standard & Poor's 500 Index) declined almost 50% from its peak value attained in March 2000, reaching a bottom in March 2003. The stock market recovery that began in April 2003 contributed to very favorable rate of return for the System. The rate of return on the fair market value of assets as of June 30, 2004 was 11.2% versus 5.4% for the period ended June 30, 2003. The rate of return on the actuarial value of assets was 2.3% and (2.5%) respectively versus the expected rate of return of 7.50% for both years.

The actuarial value of assets, which is used to determine the City of Norfolk, Virginia's (the "City") contribution rate for the following fiscal year, is determined using a method that is designed to smooth the impact of market fluctuations.

Unlike the market value, which immediately reflects all realized and unrealized appreciation and depreciation during the year, the actuarial value recognizes annual appreciation and depreciation over a three-year period. The net gain during the fiscal year ended June 30, 2004 will be recognized gradually, a portion recognized in this year's asset value and the remainder recognized over the next two years. Thus, the 2.3% rate of return on the actuarial value of assets during the last year actually reflects a portion of last year's return on the market value, plus a portion of the market performance during prior two years.

OVERVIEW OF FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the System's basic financial statements which include the following components:

1. Fund financial statements,
2. Notes to the financial statements,
3. Required supplementary information.

The information available in each of these sections is briefly summarized as follows:

1. **Fund Financial Statements**--A statement of fiduciary net assets and a statement of changes in fiduciary net assets are presented as of June 30, 2004. These financial statements reflect the resources available to pay benefits to retirees and other beneficiaries as of year end, and as well as changes in those resources during the year.
2. **Notes to the Basic Financial Statements**--The financial statement notes provide additional information that is essential to the full understanding of the data provided in the Fund Financial Statements. Information available in the notes to the financial statements includes:
 - Note 1 discloses significant accounting policies
 - Note 2 provides description of the system and the funding policy as well as a description of member contributions and benefits
 - Note 3 discusses contributions required and contributions made
 - Note 4 discusses System investments and deposits and includes a table showing investments categorized as to risk
 - Note 5 reveals transactions with City of Norfolk
 - Note 6 income tax status
 - Note 7 change in benefit provisions

FINANCIAL SECTION

3. **Required Supplementary Information**—This information shows the System's funding progress, annual contributions as a percentage of required contributions, lists the various actuarial assumptions as well as provides detail regarding administrative and investment expenses.

Net Assets – Employees' Retirement System of the City of Norfolk, Virginia:

As of:	June 30, 2004 (millions)	June 30, 2003 (millions)
Total assets	\$ 839.6	\$ 788.1
Total liabilities	23.5	37.9
Net assets	<u>\$ 816.1</u>	<u>\$ 750.2</u>

Change in Net Assets – Employees' Retirement System of the City of Norfolk, Virginia:

As of:	June 30, 2004	June 30, 2003
Additions:		
Net depreciation in fair value of investments	\$ 69,879,895	\$ 24,190,844
Dividends and interest	14,748,946	16,737,226
Contributions	23,469,744	21,390,048
Investment expense	(2,394,156)	(1,957,714)
Total additions	<u>\$105,973,951</u>	<u>\$ 60,773,012</u>
Deductions:		
Benefit payments	\$ 37,259,195	\$ 35,081,656
Refunds of contributions	47,622	87,063
Beneficiary payments	2,284,961	2,247,037
Administrative fees	470,767	524,513
Total deductions	<u>40,062,545</u>	<u>37,940,269</u>
Increase (decrease) in net assets	<u>\$ 65,911,406</u>	<u>\$ 22,832,743</u>

CONTACTING THE SYSTEM'S FINANCIAL MANAGEMENT

The system's financial statements are designed to present users with a general overview of the System's finances and the prudent exercise of the Board's oversight. If you have any questions regarding this report or need additional financial information, please contact the Employees' Retirement System of the City of Norfolk, 810 Union Street, Room 309, Norfolk, Virginia 23510. This report may also be accessed at www.norfolk.gov/finance/retirement.

Employees' Retirement System of the City of Norfolk

(A Pension Trust Fund of Norfolk, Virginia)

Statement of Plan Net Assets

June 30, 2004

Assets:

Cash and short-term investments	\$ 59,553,103
Receivables	
Employer contribution	23,469,744
Accrued investment income	1,999,363
Due from broker for securities sold	<u>15,045,225</u>

Total receivables 40,514,332

Investments, fair value	
United States Government securities	84,320,806
Corporate bonds and debentures, including obligations of national mortgage associations	98,037,091
Common stocks	105,911,057
Domestic equity funds	390,264,177
Domestic bond fund	<u>60,976,451</u>

Total investments 739,509,582

Total assets \$ 839,577,017

Liabilities and net assets:

Accounts payable	\$ 359,403
Due to broker for securities purchased	<u>23,097,285</u>

Total liabilities 23,456,688

NET ASSETS HELD IN TRUST FOR PENSION BENEFITS \$ 816,120,329

(A schedule of funding progress is presented on page 18)

See accompanying notes to financial statements

FINANCIAL SECTION

Employees' Retirement System of the City of Norfolk
(A Pension Trust Fund of Norfolk, Virginia)
Statement of Changes in Plan Net Assets
June 30, 2004

Additions:

Net appreciation in fair value of investments	\$ 69,879,895
Interest	9,770,728
Dividends	4,978,218
Other	<u>269,522</u>
Employer Contributions	84,898,363
Less investment expense	<u>23,469,744</u>
	<u>(2,394,156)</u>
Total additions	105,973,951

Deductions:

Benefits paid directly to participants	\$ 37,259,195
Refunds of contributions	47,622
Beneficiary payments	2,284,961
Administrative fees	<u>470,767</u>
Total deductions	<u>40,062,545</u>
Net increase	65,911,406

Net assets held in trust for pension benefits, beginning of year 750,208,923

**NET ASSETS HELD IN TRUST FOR PENSION BENEFITS,
END OF YEAR**

\$816,120,329

See accompanying notes to financial statements

Employees' Retirement System of the City of Norfolk
(A Pension Trust Fund of Norfolk, Virginia)
Notes to Financial Statements
For the Year Ended June 30, 2004

NOTE 1 - Significant accounting policies

Basis of accounting – The financial statements of the Employees' Retirement System of the City of Norfolk (the "System") are prepared using the accrual basis of accounting. Employer contributions are recognized when due. Benefits and refunds are recognized when due and payable in accordance with the terms of the Plan.

The System has applied the provisions of Governmental Accounting Standards Board Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans* ("GASB 25") in the preparation of these financial statements. GASB 25 establishes financial reporting standards for defined benefit pension plans and for the notes to the financial statements of defined contribution plans of state and local governmental entities and requires two basic financial statements, a statement of plan net assets and a statement of changes in plan net assets, that provide current financial information about plan assets and financial activities. Actuarially determined information, from a long-term perspective, about the funded status of the plan and related funding progress is presented in two required schedules, a schedule of funding progress and a schedule of employer contributions. GASB 25 also establishes certain parameters for the measurement of all actuarially determined information included in financial reports of defined benefit pension plans.

Investment valuation method – Investments are stated at fair value. Short-term investments are recorded at cost, which approximates fair value. Securities traded on a national securities exchange are valued at the last reported sales price on the last business day of the System's fiscal year. Investments that do not have an established market are reported at estimated fair value. Purchases and sales of securities traded but not yet settled at year-end are recorded as due to broker for securities purchased and due from broker for securities sold, respectively.

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

Component Unit – The System is included as a discrete component unit in the Comprehensive Annual Financial Report of the City of Norfolk as a Pension Trust Fund.

NOTE 2 – Description of the plan

The System is the administrator of a single-employer noncontributory defined benefit plan that covers substantially all employees of the City of Norfolk, Virginia, excluding School Board employees who are covered by the Virginia Retirement System. Although the System presents separate financial statements, it is also included as a component unit in the City of Norfolk's Comprehensive Annual Financial Report as a pension trust fund.

FINANCIAL SECTION

NOTE 2 – Description of the plan (continued)

The types of employees covered and current membership as of June 30, 2004 and 2003 consists of the following:

	<u>2004</u>	<u>2003</u>
Retirees and beneficiaries receiving benefits:		
General	1,953	1,915
Public safety	829	795
Terminated plan members entitled to but not yet receiving benefits:		
General	686	662
Public safety	122	116
Active plan members:		
Fully vested:		
General	1,873	1,877
Public safety	929	950
Nonvested:		
General	788	767
Public safety	299	272
Total	<u>7,479</u>	<u>7,354</u>

The System provides retirement benefits as well as death and disability benefits. All benefits vest after 5 years of creditable service effective January 1, 1997. Employee eligibility requirements are as follows (see Note 3):

Retirement (for employees who became members prior to July 1, 1980): Normal retirement is the earlier of age 60 or after completion of 30 years of credited service for general employees, and the earlier of age 55 or after the completion of 25 years of credited service for public safety employees. The normal service retirement benefit per annum is equal to 2.0 percent of average final compensation (average of the three highest years of compensation) times years of creditable service, with service limited to 35 years. Public safety employees accrue benefits at 2.5 percent of average final compensation times years of creditable service, not to exceed 65% of average final compensation. Mandatory retirement is age 62 for public safety employees.

Retirement (for employees who became members on or after July 1, 1980 but prior to January 1, 1997): Normal retirement is the earlier of age 60 or after completion of 30 years of credited service for general employees, and age 55 or after the completion of 25 years of credited service for public safety employees. The normal service retirement benefit per annum for general employees is equal to 1.75 percent of average final compensation times years of creditable service, with service limited to 35 years. Public safety employees accrue benefits at 2.5 percent of average final compensation times years of creditable service, not to exceed 65% of average final compensation.

NOTE 2 – Description of the plan (concluded)

The System also provides for ordinary death and disability benefits and accidental death and disability benefits. Ad hoc cost-of-living adjustments ("COLAs") are provided at the discretion of the City Council. Participants should refer to the Plan document for a complete description of these benefits.

The Employees' Retirement System is established by Section 37 of the Code of the City of Norfolk, Virginia, 1979, as amended 1997. The benefit provisions of the Plan are also determined by this Code section.

NOTE 3 – Contributions required and contributions made

Significant assumptions used to calculate contribution requirements are the same as those used to calculate the actuarial accrued liability. Normal cost is funded on a current basis. Periodic contributions for normal cost are based on the level percentage-of-payroll method. The unfunded actuarial accrued liability as of June 30, 2004 and 2003 is \$84,200,126 and \$52,733,559, respectively. The funding strategy for normal cost should provide sufficient resources to pay employee pension benefits on a timely basis.

Section 37 of the Code of the City of Norfolk, Virginia, 1979, as amended 1997 establishes the authority under which the employer's obligation to contribute to the plan is established or may be amended. Contribution requirements are actuarially determined at the end of each fiscal year and paid by the City of Norfolk in the ensuing year. The contribution requirement of \$23,469,744 for the year ended June 30, 2004 was based on 9.4% of covered payroll for general employees and 24.3% of covered payroll for public safety employees. The contribution requirement of \$17,046,924 for the year ended June 30, 2003 was based on 5.8% of covered payroll for general employees and 19.2% of covered payroll for public safety employees.

Voluntary contributions were discontinued in 1979 and have been accumulated thereafter with interest at a rate of 7%. Such contributions are refundable to members who terminate before becoming eligible for retirement benefits. At retirement, members' contributions plus accumulated interest are refunded. Such amounts totaled \$316,409 and \$345,772 at June 30, 2004 and 2003, respectively.

NOTE 4 – Investments and deposits

Deposits – At June 30, 2004 and 2003, the carrying amounts of the System's cash deposits with banks and investment companies were \$1,224,899 and \$2,294,065, respectively, and the bank and investment company balances were \$1,201,351 and \$1,799,691, respectively. The entire bank balance was covered by federal depository insurance, commercial insurance or collateralized in accordance with the Virginia Security for Public Deposits Act. Under the Act, banks holding public deposits in excess of the amounts insured by FDIC must pledge collateral in the amount of 50% of excess deposits to a collateral pool in the name of the State Treasury Board. The State Treasury Board is responsible for monitoring compliance with the collateralization and reporting requirements of the Act and for notifying local governments of compliance by banks.

FINANCIAL SECTION

NOTE 4 – Investments and deposits (continued)

Investments – The Code of Virginia authorizes the System to invest in certificates of deposit with national banks located within the Commonwealth of Virginia, obligations of the United States or its agencies, bankers' acceptances, repurchase agreements, "prime quality" commercial paper, common stock, and certain other qualified investments. The System's investments are recorded at fair value in the financial statements.

The System's investments at June 30, 2004 and 2003 are categorized in the following table to give an indication of the level of credit risk assumed by the System at year-end. Category 1 includes investments that are insured or registered or for which the securities are held by the System or its safekeeping agent in the System's name. Category 2 includes uninsured or unregistered investments for which the securities are held by the broker's or dealer's trust department or safekeeping agent in the System's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the broker or dealer, or by its trust department or safekeeping agent but not in the System's name. All of the System's investments fall under Category 1. The System's investments at June 30, 2004 and 2003 are as follows:

2004			
	Cost Category 1	Cost	Fair Value
U.S. Government securities	\$ 85,726,514	\$ 85,726,514	\$ 84,320,806
Corporate bonds and debentures, including commercial paper classified as cash and short-term investments	146,665,621	146,665,621	159,013,542
Common stocks	58,805,935	58,805,935	496,175,234
	<u>\$ 291,198,070</u>	<u>291,198,070</u>	<u>739,509,582</u>
Money market investments included in cash and short-term investments		59,553,103	59,553,103
		350,751,173	799,062,685
Less: funds classified as cash equivalents		59,553,103	59,553,103
Total investments		<u>\$ 291,198,070</u>	<u>\$ 739,509,582</u>

2003			
	Cost Category 1	Cost	Fair Value
U.S. Government securities	\$ 35,153,484	\$ 35,153,484	\$ 36,226,765
Corporate bonds and debentures, including commercial paper classified as cash and short-term investments	152,122,040	152,122,040	185,111,690
Common stocks	222,798,397	222,798,397	220,509,210
	<u>\$ 410,073,921</u>	<u>410,073,921</u>	<u>441,847,665</u>
State Street Conservative Fund		175,533,847	239,162,238
State Street Global Advisors Bond Market Fund		32,510,790	44,920,702
Money market investments included in cash and short-term investments		33,554,910	33,554,910
		651,673,468	759,485,515
Less: funds classified as cash equivalents		33,554,910	33,554,910
Total investments		<u>\$ 618,118,558</u>	<u>\$ 725,930,605</u>

FINANCIAL SECTION

NOTE 4 – Investments and deposits (concluded)

The System's investments, (including investments bought and sold, as well as held throughout the year), appreciated (depreciated) in fair value as determined by quoted market prices as follows for the years ended June 30, 2004 and 2003:

	2004	2003
U.S. Government and government agencies securities	\$ (2,403,004)	\$ 3,904,211
Corporate bonds and debentures	(6,046,015)	15,582,110
Common stocks and equity funds	78,328,914	4,704,523
	<u>\$ 69,879,895</u>	<u>\$ 24,190,844</u>

The System invests in certain derivatives including real estate mortgage investment conduits and collateralized mortgage obligations. Those securities are included in reported investments. Investments in derivatives with a cost of \$41,099,386 and \$40,673,432 and a market value of \$37,847,353 and \$41,387,540 were held at June 30, 2004 and 2003, respectively.

NOTE 5 – Transactions with City of Norfolk

Effective January 1, 1992, the System began reimbursing the City for all administrative costs related to the System's operations. The costs reimbursed for the years ended June 30, 2004 and 2003 were \$354,027 and \$289,035, respectively.

NOTE 6 – Income tax status

The Internal Revenue Service has ruled that the Plan qualifies under Section 401-1(b)(3) of the Internal Revenue Code and is, therefore, not subject to tax under present income tax laws. Although the Plan has been amended since receiving a determination letter from the Internal Revenue Service, the Plan administrator and the Plan's tax counsel believes that the Plan is designed and is currently being operated in compliance with the applicable requirements of the Internal Revenue Code.

NOTE 7 – Changes in benefit provisions

The June 30, 2002 benefit obligations reflect the following changes in the benefit provisions:

- (a) City council members are treated by the System as members of the public safety group of employees, rather than the general group of employees. This change increased benefit obligations by \$110,843.
- (b) Eligibility for ordinary death benefits was changed from 10 years of service or eligibility for normal service retirement to also include any member who has less than 10 years but is eligible for early service retirement. This change increased benefit obligations by \$27,659.
- (c) Retirees and beneficiaries as of December 31, 2001 were granted a permanent 2% supplemental benefit increase effective July, 2002. This change increased benefit obligations by \$6,380,344.

Employees' Retirement System of the City of Norfolk

(A Pension Trust Fund of Norfolk, Virginia)

Required Supplementary Actuarial Information

For Year Ended June 30, 2004

Historical trend information about the System is presented herewith as required supplementary information. An actuarial valuation is performed annually at fiscal year end. Information from the seven most recent valuations is presented below. This information is intended to help users assess the System's funding status, assess progress made in accumulating assets to pay benefits when due, and make comparisons with other public employee retirement systems.

Schedule of Funding Progress (\$ in millions):

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Projected Unit Credit (b)	Funding Excess (Shortage) (a-b)	Funded Ratio (a/b)	Covered Payroll (c)	Funding Excess (Shortages) as a Percentage of Covered Payroll ((a-b)/c)
June 30, 2004	761.5	845.7	(84.2)	90.0%	157.7	-53.4%
June 30, 2003	760.5	813.2	(52.7)	93.5%	152.1	-34.6%
June 30, 2002	798.1	784.7	13.4	101.7%	150.7	8.9%
June 30, 2001	838.1	742.6	95.5	112.9%	144.2	66.2%
June 30, 2000	826.4	628.2	198.2	131.5%	129.9	152.6%
June 30, 1999	767.8	601.4	166.4	127.7%	129.0	129.0%
June 30, 1998	694.2	569.9	124.3	121.8%	122.2	101.8%

Schedule of Employer Contributions:

Fiscal Year Ended June 30	Annual Required Contribution	Percentage Contributed
2004	\$ 23,469,744	100 %
2003	21,390,048	100
2002	-	100
2001	-	100
2000	-	100
1999	3,456,936	100
1998	10,158,768	100

FINANCIAL SECTION

Actuarial Assumptions:

Actuarial cost method	Projected unit credit cost method
Amortization method	Level dollar closed
Remaining amortization period	Weighted average of 14.5 years
Asset valuation method	3-year smoothed market
Actuarial assumptions:	
Assumed inflation rate	3.5%
Investment rate of return	5.4% per annum, compounded annually
Projected salary increases*	Average salary increases of 5.35%, compounded annually (This reflects an assumption of a range of salary increases from 7.6% at age 20 to 4.6% at age 69.)
*Includes inflation at 3.5%	
Cost-of-living adjustments	None
Separation from active service	Assumed rates of separation from service vary depending on the age of the employee and whether the employee is a general employee or public safety employee. 1995 Mellon mortality tables with ages rated forward 1 year for members and 2 years for beneficiaries. Special mortality tables are used for disability retirements.
Marital status	65% of the general employees and 80% of the public safety employees are assumed to be married, with the males three years older than females.

The actuarial assumptions above are based on the presumption that the System will continue indefinitely. If the System were to terminate, different actuarial assumptions and other factors might be applicable in determining the actuarial accrued liability.

FINANCIAL SECTION

Employees' Retirement System of the City of Norfolk
(A Pension Trust Fund of Norfolk, Virginia)
Schedule of Administrative Expenses
June 30, 2004

Personal Services:

Staff salaries	\$229,840	
Benefits	<u>51,200</u>	
Total Personal Services		\$281,040

Professional Services:

Actuarial Fees	63,182	
Medical Examinations	<u>4,910</u>	
Total Professional Services		68,092

Communication:

Printing	4,875	
Travel & Training	34,111	
Postage & Shipping	<u>10,777</u>	
Total Communication		49,763

Data Processing:

IT Services	22,942	
Computer Equipment & Supplies	<u>11,788</u>	
Total Data Processing		34,730

Miscellaneous:

Supplies & Equipment	2,569	
Maintenance & Repairs	1,888	
Other	<u>32,685</u>	
Total Miscellaneous		37,142

Total Administrative Expenses		<u>\$470,767</u>
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Employees' Retirement System of the City of Norfolk
(A Pension Trust Fund of Norfolk, Virginia)
Schedule of Investment Expenses
June 30, 2004

Investment Manager Fees	<u>1,952,505</u>	
Total Investment Manager Fees		\$1,952,505

Schedule of Payments to Custody and Investment Consultant

Custody Fees	149,716	
Investment Consultant Fees	<u>291,935</u>	
Total Custody and Investment Consultant Fees		<u>441,651</u>
Total Investment Expenses		<u>\$2,394,156</u>

Investment Section

Investment Performance, Policy, Statistics and Activity

In the investment of public funds, adequate funding of employee retirement benefits at a reasonable and affordable cost is a paramount concern. An appropriate balance must be struck between risks taken and returns sought to ensure the long term health of the System. The System has adopted an investment policy which works to control the extent of the downside risk to which assets are exposed while maximizing the potential for long-term increase in the value of the assets.

Investment Objectives

The Board of Trustees has adopted Investment Policies and Guidelines, which outline the System's investment goals and objectives. This comprehensive document contains a statement of Investment Goals and Objectives, General Investment Principles and Guidelines.

The Plan's general investment goals are broad in nature. The primary objectives are to efficiently allocate and manage the assets, dedicated to the payment of Plan benefits and administrative expenses. The following goals, consistent with the above-described purpose, are adopted:

- The overall goal of System's investment portfolio is to provide a retirement benefit for the employees of the City of Norfolk, Virginia. This will be accomplished through a carefully planned and executed long-term investment program.
- The total portfolio over the long term will be expected to earn a return that equals or exceeds:
 1. The rate of inflation, as measured by the Consumer Price Index, plus 2.5% per year;
 2. The return of a target policy index ("Target Policy");
 3. The 33rd percentile return of a universe of comparably managed balanced funds;
 4. For the aggregate equity and fixed income components of the fund, the return of the S&P 500 and the Lehman Aggregate Bond indices, respectively; and
 5. For the aggregate equity and fixed income components of the fund, the 33rd percentile return of a universe of comparably managed equity and fixed income funds, respectively.
 6. The actuarially assumed investment rate of return.

Asset Allocation

The System adopts and implements an asset allocation policy that is predicated on a number of factors, including:

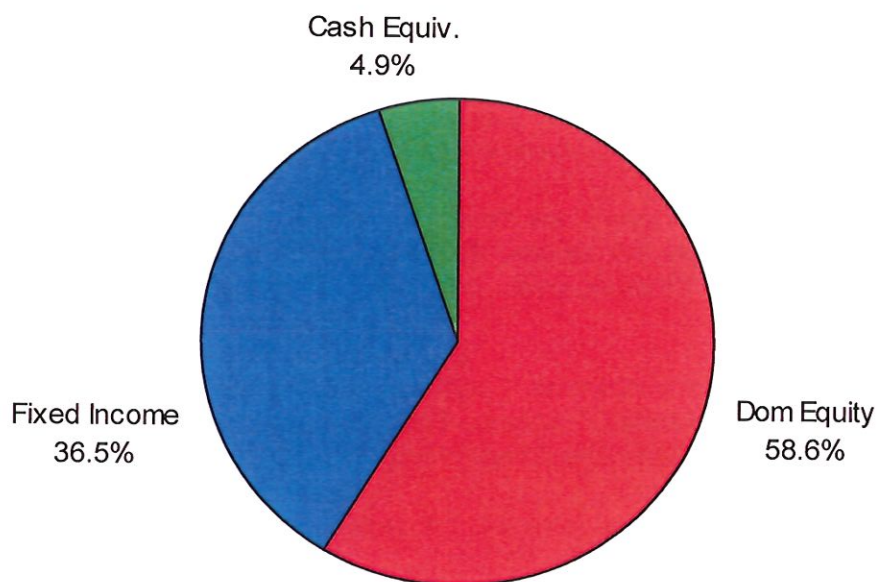
- Historical and expected long-term capital market risk and return behavior;
- Projected assets, liabilities, benefit payments and contributions provided by System's actuary;
- An assessment of future economic conditions, including inflation and interest rate levels; and
- The specific investment objectives set forth in the Investment Policy Statement.

The System will be diversified both by asset class (e.g., common stocks, bonds, cash) and within asset classes (e.g., within common stocks by economic sector, industry, quality and

INVESTMENT SECTION

market capitalization). The purpose of diversification is to provide reasonable assurance that no single security or class of securities will have a disproportionate impact on the total System.

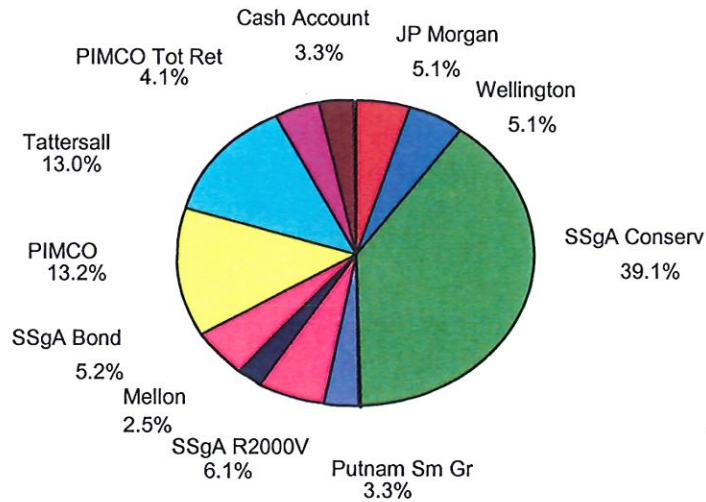
Asset Allocation as of June 30, 2004



Domestic Equity	\$463,937,951
Fixed Income	289,520,820
Cash Equivalent	<u>38,818,126</u>
Total	<u>\$792,276,897</u>

INVESTMENT SECTION

Investment Managers and Investment Assignments as of June 30, 2004



JP Morgan	\$ 40,084,346
Wellington	40,749,941
SSgA Conserv	309,871,209
Putnam Sm Gr	26,420,988
SSgA R2000V	48,088,975
Mellon	19,640,623
SSgA Bond	41,332,579
PIMCO	104,553,591
Tattersall	103,033,170
PIMCO Tot Ret	32,394,942
Cash Account	26,109,533
Total:	<u>\$792,276,897</u>

Asset Allocation Comparison as of June 30, 2004

	Equity Commitment	Fixed Income Commitment
Total Fund	58.6%	36.5%
Median Total Fund	61.6%	30.6%
Median Public fund	61.0%	32.4%

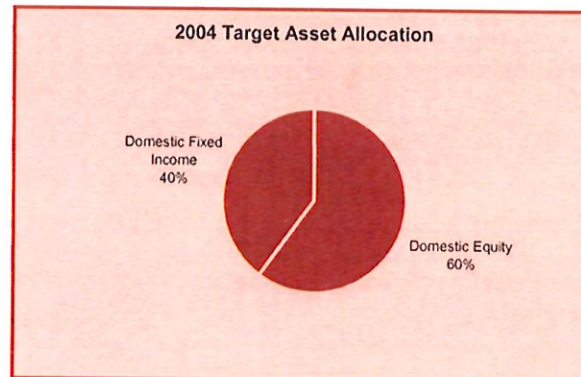
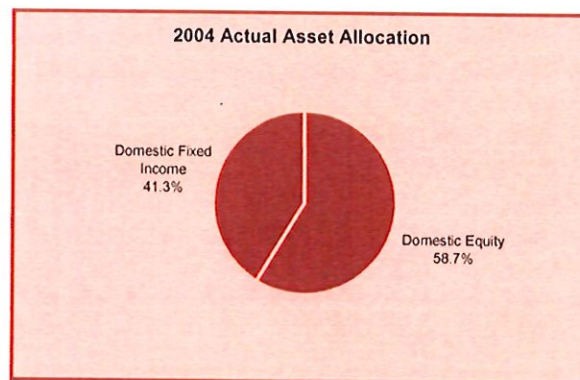
INVESTMENT SECTION

TARGET ASSET ALLOCATION

The target asset allocation for the investment portfolio is determined by the Board of Trustees to facilitate the achievement of the investment program's long-term investment objectives within the established risk parameters. Due to the fact that the allocation of funds between asset classes may be the single most important determinant of the investment performance over the long run, the System's assets shall be divided into the following asset classes:

Asset Class	Minimum Percent	Maximum Percent	Target Percent
Domestic Equity	55.0%	62.5%	60.0%
Domestic Fixed Income	37.5%	45.0%	40.0%

Formal asset allocation studies will be conducted at least every five years, with annual evaluations of the validity of the adopted asset allocation based on updated return projections. Any change in capital market assumptions or liabilities will require consideration of revision to the asset allocation policy. The System is currently in the process of reviewing existing asset allocation percentages through an extensive asset/liability study conducted by the external investment consultant.



INVESTMENT SECTION

Investment Performance Summary

For the Periods Ended June 30, 2004

Account	Current	Annualized			
		2 Year	3 Year	4 Year	5 Year
Equity					
JP Morgan Investments	19.2%	9.0%	(2.0%)	N/A	N/A
S&P 500	19.1%	9.3%	(0.7%)	(4.4%)	(2.2%)
Wellington Management Co.	17.5%	10.7%	(1.7%)	N/A	N/A
S&P 500	19.1%	9.3%	(0.7%)	(4.4%)	(2.2%)
SSgA Conservative Fund	19.0%	9.4%	(0.6%)	(4.4%)	(2.1%)
S&P 500	19.1%	9.3%	(0.7%)	(4.4%)	(2.2%)
Putnam Small Cap Growth	23.8%	11.4%	(2.8%)	(8.1%)	5.0%
Russell 2000 Growth	31.5%	15.1%	(0.2%)	(6.6%)	(0.5%)
SSgA Russell 2000 Value Fund	N/A	N/A	N/A	N/A	N/A
Russell 2000 Value	35.2%	14.0%	12.2%	16.6%	12.8%
Total Domestic Equity	19.6%	9.1%	(2.1%)	(5.4%)	(2.2%)
Domestic Equity Policy Index*	3.9%	20.9%	20.9%	0.2%	(1.0%)
S&P 500	19.1%	9.3%	(0.7%)	(4.4%)	(2.2%)
Russell 3000	20.5%	10.2%	0.1%	(3.6%)	(1.1%)
Fixed Income					
Mellon Aggregate Bond Fund	0.3%	N/A	N/A	N/A	N/A
Lehman Aggregate	0.3%	5.2%	6.4%	7.6%	6.9%
SSgA Bond Index Fund	0.2%	5.2%	6.4%	7.6%	7.0%
Lehman Aggregate	0.3%	5.2%	6.4%	7.6%	6.9%
PIMCO	0.2%	5.3%	6.4%	7.5%	7.0%
Lehman Aggregate	0.3%	5.2%	6.4%	7.6%	6.9%
Tattersall Advisory Group	0.6%	5.7%	6.7%	8.0%	7.3%
Lehman Aggregate	0.3%	5.2%	6.4%	7.6%	6.9%
PIMCO Total Return	1.0%	N/A	N/A	N/A	N/A
Lehman Aggregate	0.3%	5.2%	6.4%	7.6%	6.9%
Total Fixed Income	0.5%	5.5%	6.5%	7.7%	7.0%
Lehman Aggregate	0.3%	5.2%	6.4%	7.6%	6.9%
Total Fund	11.4%	8.5%	2.8%	1.5%	2.9%
Total Fund Policy Index**	11.4%	9.0%	4.1%	2.5%	3.2%
Total Fund Proposed Policy Index***	12.1%	9.5%	4.5%	3.0%	3.8%

* Domestic Equity Policy Index = 87.5% S&P 500, 12.5% Russell 2000.

** Total Fund Policy Index = 60% S&P 500, 40% Lehman Aggregate.

*** Total Fund Proposed Policy Index = 60% Russell 3000, 40% Lehman Aggregate.

Investment returns are shown net of investment management fees. The investment returns shown elsewhere in this report are net of all expenses paid by the system (investment management fees, custody and consultant fees, and administrative expenses).

INVESTMENT SECTION

Schedule of Broker Commissions

Broker selection is the responsibility of individual investment managers. Transactions and commission cost are monitored by the State Street Bank (Custodian), investment consultant, and Chief Investment Officer.

Following is a list of brokers who received commissions of \$10,000 or more during fiscal year 2004. A complete schedule of all commissions paid is available from the Retirement Office.

Broker	Number of Shares	Total Commision \$	Commission \$ Per Share
State Street Brokerage	5,023,630	75,574	0.015
UBS Warburg	1,218,757	69,104	0.057
Merrill Lynch Pierce Fenner & Smith	936,806	43,332	0.046
Morgan Stanley Co., Inc.	644,806	28,072	0.044
Goldman Sachs	585,864	26,419	0.045
Credit Suisse First Boston	465,210	19,402	0.042
Bank of America	409,636	16,882	0.041
Citigroup Global Markets	389,100	16,752	0.043
Investment Tech	465,632	12,340	0.027
Lehman Brothers	260,224	12,256	0.047
J.P. Morgan	221,600	10,796	0.049
S.G. Cowen Securities	226,112	10,555	0.047

INVESTMENT SECTION

List of Largest Assets Directly Held As of June 30, 2004

Ten Largest Stock Holdings (by fair market value)

Stock	Shares	Fair Value
CITIGROUP INC	62,001	\$2,883,046
MICROSOFT CORP	84,900	2,424,744
GENERAL ELECTRIC CO (US)	67,000	2,170,800
PFIZER INC	61,840	2,119,875
EXXON MOBIL CORP	39,498	1,754,106
WAL MART STORES	29,800	1,572,248
GILLETTE	36,600	1,551,840
CISCO SYSTEMS	64,200	1,521,540
BANK OF AMERICA CORP	16,100	1,362,382
ALTRIA GROUP INC	26,200	1,311,310

Ten Largest Bond Holdings (by fair market value)

Bond	Par	Fair Value
US TREAS NTS 5.000% DTD 15AUG2001 DUE 15AUG2011	31,290,000	\$33,267,486
POOLED SHORT TERM	11,433,328	11,433,327
UNITED STATES TREAS NTS	7,500,000	8,199,036
UNITED STATES TREAS BONDS 6% 15FEB26 USD1000	7,300,000	8,031,769
US TREAS NTS 3.000% DTD 15FEB2003 DUE 15FEB2008	7,500,000	7,482,759
US TREAS NTS DTD 03/31/04 1.50% 03/31/2006	7,500,000	7,392,378
GNMA TBA 5.000% DTD 01JUN2003 DUE 01JUL2033	7,000,000	6,783,980
US TREAS BONDS 7.50% DTD15OCT86 DUE15NOV2016	5,400,000	6,710,627
HBOS TREAS SVCS PLC	3,100,000	3,097,251
US G TREAS NT 3.625% DTD 15JAN1998 DUE 15JAN2008	2,658,593	2,949,418

A complete list of portfolio holdings is available upon request.

Actuarial Section



December 14, 2004

Board of Trustees
Employees' Retirement System
of the City of Norfolk
Norfolk, Virginia 23510

Members of the Board:

Actuarial valuations of the Employees' Retirement System of the City of Norfolk are performed annually. The results of the latest actuarial valuation of the System, which we have prepared as of June 30, 2004, are summarized in this letter.

The valuation reflects the benefits in effect on the valuation date, and was prepared on the basis of the data submitted by the City and the actuarial assumptions as adopted by the Board of Trustees, including a valuation interest rate assumption of 7½% per annum, compounded annually.

The actuarial assumptions and methods used for funding purposes comply with the parameters set forth in Statement No. 25 of the Governmental Accounting Standards Board.

Financing Objective and Contribution Appropriation

The financing objective of the System is to:

- (a) fully fund the normal cost contribution for the current year determined under the funding method; and
- (b) liquidate the unfunded accrued liability based on level accrued liability contributions payable over a closed amortization period of 20 years.

The contribution appropriated for the fiscal year ended June 30, 2004 was determined based on the results of the June 30, 2003 valuation. The contribution amount is \$23,469,744.

The results of the June 30, 2004 valuation determine the contribution appropriation for the fiscal year ending June 30, 2005, which will be presented in our valuation report subject to your approval.

As of June 30, 2004, the System's accrued liability was 90.0% funded based on the actuarial value of assets, including the contribution for the fiscal year ended June 30, 2004. The accrued liability was 96.5% funded based on the market value of assets.

Included in the valuation report are contribution and funding progress schedules prepared by the actuary.

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Board of Trustees
Employees' Retirement System
of the City of Norfolk
December 14, 2004
Page 2

Assets and Participant Data

The City reported the individual data for members of the System as of the valuation date to the actuary. While we did not verify the data at their source, we did perform tests for internal consistency and reasonability in relation to the data submitted for the previous valuation.

The amount of current assets in the trust fund taken into account in the valuation was based on statements prepared for us by the City.

Actuarial Assumptions and Methods

The current actuarial assumptions used for valuation purposes were adopted by the Board of Trustees and were first effective with the June 30, 2001 actuarial valuation. The most recent study of the plan's experience, used in developing the current actuarial assumptions, was based on a period from July 1995 to June 2000. In our opinion, the actuarial assumptions used in the valuation are, in the aggregate, reasonable.

Included in the valuation report is a schedule, which presents an outline of the actuarial assumptions and methods used to prepare the actuarial valuation results.

The actuarial cost method utilized is the projected unit credit method.

The valuation assets are determined as the market value less (1) 66-2/3% of the net appreciation during the preceding year, and (2) less 33-1/3% of the net appreciation during the second preceding year.

Schedules of Financial Results and Membership Data

Detailed summaries of the financial results of the valuation and membership data used in preparing the valuation are shown in the valuation report. The actuary prepared supporting schedules and required supplementary information included in the Actuarial, Financial and Statistical Sections of the Comprehensive Annual Financial Report.

To the best of our knowledge, this report is complete and accurate and has been prepared in accordance with generally accepted actuarial principles and practice.

Respectfully submitted,



Paul R. Wilkinson, A.S.A., E.A.
Director, Consulting Actuary

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SUMMARY OF ACTUARIAL ASSUMPTIONS AND METHODS

ASSUMPTIONS

INTEREST RATE: 7½% per annum, compounded annually (adopted as of June 30, 1990).

SEPARATION FROM ACTIVE SERVICE: Illustrative rates of assumed separation from service are as follows (adopted as of June 30, 2001).

GENERAL EMPLOYEES:

Age	Withdrawal	Disability*		Death**	
		Male	Female	Male	Female
20	20.35%	0.13%	0.09%	0.09%	0.03%
25	17.37	0.15	0.11	0.11	0.03
30	9.27	0.18	0.12	0.10	0.04
35	6.81	0.29	0.20	0.11	0.05
40	5.60	0.44	0.30	0.16	0.07
45	3.91	0.68	0.47	0.24	0.10
50	2.51	1.01	0.69	0.35	0.16
54	1.45	1.32	0.90	0.49	0.26
55		1.41	0.96	0.54	0.29
59		2.05	1.40	0.85	0.48

*7.5% of disabilities are assumed to be accidental

**1.5% of deaths are assumed to be accidental

Age	Early Retirement	Normal Service Retirement
40	10.00%	
45	10.00	25.00%
50	10.00	30.00
53	5.00	35.00
55	5.00	35.00
56	5.00	35.00
57	5.00	35.00
58	5.00	35.00
59		30.00
60		30.00
61		30.00
62		30.00
63		25.00
64		25.00
65		25.00
66		20.00
67		20.00
68		15.00
69		15.00
70		100.00

ACTUARIAL SECTION

Actuarial Assumptions (Continued)

FIREFIGHTERS AND POLICE:

Age	Withdrawal	Disability		Death*	
		Accidental	Ordinary	Male	Female
20	11.90%	0.03%	0.04%	0.09%	0.03%
25	7.57	0.05	0.06	0.11	0.03
30	3.43	0.07	0.09	0.10	0.04
35	1.76	0.10	0.12	0.11	0.05
40	0.95	0.25	0.18	0.16	0.07
45	0.34	0.47	0.32	0.24	0.10
50		0.79	0.55	0.35	0.16
54		1.06	0.74	0.49	0.26
55		1.13	0.79	0.54	0.29
59		1.49	1.03	0.85	0.48

*40% of deaths are assumed to be accidental

Age	Early Retirement	Normal Service Retirement
40	5.00%	25.00%
45	5.00	25.00
48	3.00	25.00
50	3.00	25.00
51		25.00
52		25.00
53		20.00
54		20.00
55		20.00
56		20.00
57		20.00
58		20.00
59		20.00
60		20.00
61		20.00
62		100.00

NOTE: Rates apply to each member based on eligibility requirements as defined in the Summary of Benefit and Contribution Provisions.

SALARY INCREASE: Effective average of 5.35% per annum, compounded annually. The components are 3½% for inflation, ¾% for national productivity and 1.1% for merit or seniority increases (adopted as of June 30, 1996). Representative values are as follows:

ACTUARIAL SECTION

Actuarial Assumptions (Continued)

Age	Annual Rate of Salary Increase
20	7.6%
25	7.1
30	6.6
35	6.1
40	5.6
45	5.1
50	4.6
55	4.6
60	4.6
65	4.6
69	4.6

DEATH AFTER RETIREMENT: The 1995 George B. Buck Mortality Tables with ages rated forward one year for members and two years for beneficiaries. Special mortality tables are used for disability retirements. (Adopted as of June 30, 2001.)

FUTURE EXPENSES: The assumed interest rate is net of the anticipated future administrative expenses of the fund.

LOADING OR CONTINGENCY RESERVES: None.

MARITAL STATUS: 65% of the general employees and 80% of the firefighters and police are assumed to be married, with the males three years older than females.

METHODS

ACTUARIAL COST METHOD: Projected unit credit cost method. Gains and losses are reflected in the unfunded accrued liability. Changes in the unfunded accrued liability due to benefit changes, assumption changes and gains or losses are amortized over a period of 20 years.

ASSET VALUATION METHOD: The valuation assets are determined as the market value less (1) 66 $\frac{2}{3}$ % of the net appreciation during the preceding year, less (2) 33 $\frac{1}{3}$ % of the net appreciation during the second preceding year. Appreciation (depreciation) is the increase (decrease) in the market value of assets during the year which is not related to the payments into, or out of, the Pension Accumulation Account other than from the purchase, sale, or exchange of securities.

DATA

CENSUS AND ASSETS: The valuation was based on members of the System as of June 30, 2004 and does not take into account future members. All census data was supplied by the Executive Secretary of the System and was subject to reasonable consistency checks. Asset data was supplied by the Executive Secretary and the accountants of the System.

ACTUARIAL SECTION

Schedule of Active Member Valuation Data

General Employees

Valuation as of June 30	Number of Active Members	Valuation Payroll	Average Salary	Percent Increase (Decrease) on Avg.
2004	2,644	100,685,330	38,081	2.6
2003	2,623	97,400,460	37,133	1.4
2002	2,631	96,381,952	36,633	3.4
2001	2,571	91,099,919	35,434	9.1
2000	2,547	82,700,316	32,470	1.2
1999	2,583	82,899,698	32,094	7.0
1998	2,623	78,661,820	29,989	1.0
1997	2,549	75,663,953	29,684	2.6
1996	2,516	72,788,796	28,930	(0.2)
1995	2,642	76,575,036	28,984	2.4

Firefighters and Police

Valuation as of June 30	Number of Active Members	Valuation Payroll	Average Salary	Percent Increase (Decrease) on Avg.
2004	1,217	57,029,081	46,860	2.1
2003	1,192	54,710,827	45,898	0.8
2002	1,192	54,292,435	45,547	4.0
2001	1,211	53,055,820	43,812	9.5
2000	1,178	47,149,684	40,025	2.4
1999	1,180	46,104,126	39,071	6.4
1998	1,186	43,541,224	36,713	2.2
1997	1,176	42,257,842	35,934	1.5
1996	1,066	37,738,064	35,402	(2.7)
1995	1,102	40,110,466	36,398	1.6

Total

Valuation as of June 30	Number of Active Members	Valuation Payroll	Average Salary	Percent Increase (Decrease) on Avg.
2004	3,861	157,714,411	40,848	2.4
2003	3,815	152,111,287	39,872	1.2
2002	3,823	150,674,387	39,413	3.4
2001	3,782	144,155,739	38,116	9.3
2000	3,725	129,850,000	34,859	1.7
1999	3,763	129,003,824	34,282	6.9
1998	3,809	122,203,044	32,083	1.3
1997	3,725	117,921,795	31,657	2.6
1996	3,582	110,526,860	30,856	(1.0)
1995	3,744	116,685,502	31,166	2.2

Norfolk Employees' Retirement System

ACTUARIAL SECTION

Retirees and Beneficiaries Added To and Removed From Rolls

Valuation as of June 30	Added to Rolls Number	Removed From Rolls Number	Rolls - EOY		
			Number	Annual Allowances	Percent Change
2004	176	104	2,782	41,670,258	7.1%
2003	167	103	2,710	38,925,660	6.9%
2002	145	118	2,646	36,427,435	6.5%
2001	159	122	2,619	34,197,362	6.8%
2000	159	122	2,582	32,031,396	3.9%
1999	139	104	2,545	30,823,527	3.4%
1998	97	84	2,510	29,813,163	3.0%
1997	98	78	2,497	28,948,057	3.1%
1996	294	30	2,477	28,073,965	39.4%
1995	141	125	2,213	20,134,668	3.3%

Note: The dollar amounts of the annual allowances added to and removed from the rolls are not included in the above table because the amounts would not reconcile with the total due to changes other than additions and deletions (COLAs, supplements, workers' compensation offsets, etc.)

Solvency Test

The System's funding objective is to meet long-term benefit obligations through contributions that remain approximately level from year to year as a percent of the members' payroll. If the contributions to the System are level in concept and soundly executed, the System will pay all promised benefits when due, thus providing the ultimate test of financial soundness. Testing for level contribution rates is the long-term test.

A short condition test is one means of checking a plan's progress under its funding program. In a short condition test, the System's present assets (cash and investments) are compared with: (1) the liabilities for future benefits to present retired lives, and: (2) the liabilities for service already rendered by active members. In a plan that has been following the discipline of level percent of payroll financing, the liabilities for future benefits to present retired members (Liability A) will be fully covered by present assets, except in rare circumstances. In addition, the liabilities for service already rendered by active members (Liability B) will be at least partially covered by the remainder of present assets.

The relationship between accrued liabilities and net assets of the System for the fiscal years ended June 30, 1995 through June 30, 2004 are presented as follows:

ACTUARIAL SECTION

Solvency Test

Valuation as of June 30	Accrued Liability For:		Actuarial Value of Assets	Portion of Accrued Liability Covered by Actuarial Value of Assets	
	(A)	(B)		(A)	(B)
	Retirees, Beneficiaries and Term Vested Members	Active Members			
2004 ⁽¹⁾	421,470,962	424,199,282	761,470,118	100.0	90.0
2003 ⁽²⁾	397,310,521	415,925,946	760,502,908	100.0	93.5
2002 ⁽³⁾	372,747,805	411,904,507	798,070,877	100.0	100.0
2001 ⁽⁴⁾	351,458,128	391,145,346	838,073,790	100.0	100.0
2000	317,658,619	310,593,786	826,438,858	100.0	100.0
1999	303,400,511	297,975,737	767,766,359	100.0	100.0
1998 ⁽⁵⁾	294,034,779	275,858,785	694,245,326	100.0	100.0
1997 ⁽⁶⁾	293,234,353	259,860,392	609,164,243	100.0	100.0
1996	278,893,712	236,203,795	534,776,924	100.0	100.0
1995	186,961,068	261,466,200	488,300,153	100.0	100.0

(1) Retirees and beneficiaries as of June 30, 2003 were granted a permanent 1.5% supplemental benefit increase effective July, 2004.

(2) Retirees and beneficiaries as of June 30, 2003 were granted a permanent 1% supplemental benefit increase effective July, 2003.

(3) City Council Members on or after July 1, 2001 are granted the same benefits as public safety employees. Eligibility for ordinary death benefits was extended to include any member who has less than 10 years of service and is eligible for early retirement. Retirees and beneficiaries as of December 31, 2002 were granted a permanent 2% supplemental benefit increase effective July, 2002.

(4) Board adopts changes in demographic assumptions per actuarial experience review of the System for the five year period ending June 30, 2000. The following amendments were also adopted:

- a) The benefit formula for general employees who became members after June 30, 1980 was changed to 1.75% of AFC.
- b) The benefit formula for police and firefighters was changed to 2.5% of AFC times years of service not to exceed 65% of AFC.
- c) Eligibility for normal service retirement for general employees who became members after June 30, 1980 was changed to the earlier of age 60 or the age at which the member has at least 30 years of service.
- d) The additional monthly benefit payable to qualified members earning a pension under \$500 became permanent and payable by the retirement system.
- e) Retirees and beneficiaries as of December 31, 2000 were granted a permanent 3% supplemental benefit increase.

(5) Includes the anticipated impact of Resolution 952 regarding the clarification of the City Manager's eligibility for a normal retirement allowance upon attaining age 55 and the % of average final compensation(AFC) to be credited for each year of service.

(6) Includes the anticipated impact of a permanent 2% COLA increase to retirees effective January 1, 1998.

ACTUARIAL SECTION

**Analysis of Financial Experience
For the Year Ended
June 30, 2004**

1. Unfunded (Overfunded) Accrued Liability at June 30, 2003	\$ 52,733,559
2. Interest at 7½%	3,955,017
3. Reduction in Unfunded Position Due to Amortization Charges	<u>(3,296,210)</u>
4. Expected Unfunded (Overfunded) Accrued Liability at June 30, 2004	\$ 53,392,366
5. Actual Unfunded (Overfunded) Accrued Liability at June 30, 2004	84,200,126
6. Increase (Decrease) in Unfunded Position from Expected (5) – (4)	\$ 30,807,760
7. Reasons for Increase (Decrease):	
– System Amendments	\$ 5,278,313
– Experience (Gains) Losses	
(i) Loss from Investment Return on Actuarial Value of Assets	\$ 38,521,813
(ii) Gain from Salary Increases Less Than Expected	(3,706,119)
(iii) Net Gain from Other Liability Sources	<u>(9,286,247)</u>
	<u>25,582,553</u>
– Total	\$ 30,807,760

SUMMARY OF BENEFIT AND CONTRIBUTION PROVISIONS

The following is intended to summarize the key benefits valued in this valuation. Members of the System and other parties should not rely on this summary as a substitute for or interpretation of the laws and ordinances of the Norfolk City Code covering this retirement plan.

Membership:

Any permanent regular full-time employee entering the service of the City is required to become a member of the Retirement System. Upon entering the System, members are classified according to their occupational group, either as general employees, firefighters, police officers or paramedic employees.

Paramedic employees, formerly members of the General Employees Group, were reclassified as members of Firefighters and Police effective June 9, 1992. City Council members on or after July 1, 2001 are classified as members of Firefighters and Police.

For each full calendar year beginning on or after January 1, 1997, any permanent part-time employees shall be members of and entitled to benefits in proportion to which their annual hours bear to that of full-time employees.

Benefits:

Normal Service Retirement Allowance

Eligibility	The earlier of age 60 or 30 years of creditable service for general employees. The earlier of age 55 or 25 years of creditable service for firefighters, police officers and paramedics. Mandatory retirement is age 62 for firefighters and police officers.
Employees Hired Before July 1, 1980	<p>1/50 of average final compensation for each year of creditable service.</p> <p>Effective January 1, 1997 for general employees, the maximum number of years of creditable service is the greater of 35 years or the number of years of service as of December 31, 1996.</p> <p>For firefighters, police officers and paramedics, the pension earned is 2.5% of average final compensation for each year of creditable service up to a maximum of 65% of average final compensation.</p>
Employees Hired on or After July 1, 1980	<p>1.75% of average final compensation for each year of creditable service up to a maximum of 35 years for general employees.</p> <p>For firefighters, police officers and paramedics, the pension earned is 2.5% of average final compensation for each year of creditable service up to a maximum of 65% of average final compensation.</p> <p>"Average Final Compensation" means the average annual earnable compensation for the three years of creditable service which produces the highest average. Creditable service consists of membership service plus 100% of accumulated unused sick leave for all employees except firefighters. For firefighters, 46% of unused sick leave accumulated prior to July 1, 1985 and 100% of unused sick leave accumulated on and after July 1, 1985 is included.</p>

ACTUARIAL SECTION

Summary of Plan Provisions (Continued)

Early Service Retirement Allowance

Eligibility	Within 5 years of eligibility for normal service retirement.
Amount	Accrued service retirement allowance deferred to normal service retirement age. A member may elect to receive an immediate benefit equal to the accrued service retirement allowance reduced by $\frac{1}{4}$ of 1% for each month commencement date precedes the normal retirement date for general employees and $\frac{1}{2}$ of 1% for each month commencement date precedes the normal retirement date for firefighters, police officers and paramedics.

Vested Allowance

Eligibility	5 years of creditable service.
Amount	Accrued service retirement allowance deferred to normal retirement age. If not eligible for retirement, a member may elect to leave his contributions made prior to July 1, 1972 with interest, if any, in the System until normal service retirement date.

Ordinary Disability Retirement Allowance

Eligibility	5 years of creditable service and total and permanent disability not due to an accident in the performance of duty.
Amount	Accrued service retirement allowance with a minimum of 25% of average final compensation. The minimum cannot exceed the normal service retirement allowance based on average final compensation and creditable service projected to normal service retirement date.

Accidental Disability Retirement Allowance

Eligibility	<p>Total and permanent disability as a result of an accident in the performance of duty, regardless of the length of service. Applications must be filed within 6 years from date of accident.</p> <p>The disability of a firefighter, police officer, sheriff or deputy sheriff caused by hypertension, heart disease or respiratory disease is presumed to have been suffered in the line of duty unless the contrary is shown by medical evidence.</p>
Amount	66 $\frac{2}{3}$ % of average final compensation.

ACTUARIAL SECTION

Summary of Plan Provisions (Continued)

Ordinary Death Benefit

Eligibility	Death in active service due to causes not the result of an accident in the performance of duty. Benefits are paid to a designated beneficiary or estate.
Amount	All contributions, if any, made by the member with not less than one-half of the interest credited are paid. In addition, if the member had one year of creditable service if he became a member prior to July 1, 1979 and five years of creditable service if he became a member on or after July 1, 1979, an additional lump sum benefit equal to 50% of his earnable compensation during the year immediately preceding his death is payable. If a member dies in service after the earlier of completion of ten years of service or early service retirement eligibility and if the designated beneficiary for the lump sum death benefit is the spouse, the spouse may elect to receive, in lieu of the lump sum death benefit, a monthly pension payable until death or remarriage. If the member was eligible for early or normal service retirement, the spouse's benefit is equal to one-half of the retirement allowance that would have been payable to the member had the member retired and immediately commenced payment. If the member was not eligible for early or normal service retirement, the spouse's benefit is equal to one-half of the normal service retirement allowance which would have been payable to the member if he or she had been vested, such benefit to commence at the same time as the vested benefit would have been paid to the member. If the spouse dies or remarries before the youngest unmarried child attains age 18, the pension shall continue to the date that all the children have died, married, or attained age 18, whichever occurs first. If the spouse was receiving benefits on or before June 30, 1978, payments shall continue after remarriage with no further payments after death.

Accidental Death Benefit

Eligibility	Death in active service resulting from an accident in the performance of duty within 6 years from the date of the accident. The death of a firefighter, police officer, sheriff or deputy sheriff caused by hypertension, heart disease or respiratory disease in the case of firefighters is presumed to have been suffered in the line of duty, unless the contrary is shown by medical evidence.
Amount	50% of average final compensation is payable to spouse until death or remarriage. If there is no spouse or if spouse dies or remarries, benefit is payable to children under age 18 or dependent parents. In addition, all contributions, if any, made by the member with not less than one-half of the interest credited are paid to his designated recipient or estate. If there is no spouse, a lump sum benefit equal to 50% of his earnable compensation during the year immediately preceding his death is payable.

ACTUARIAL SECTION

Summary of Plan Provisions (Continued)

Offset on Account of Workers' Compensation	All benefits paid under the provisions of any workers' compensation act or any similar law to any member or beneficiary, or to the dependents of any member or beneficiary on account of any disability or death are in such manner as the Board determines, offset against any benefits provided from City contributions to the System.
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Death Benefit After Retirement

Eligibility	Death of a retired member receiving retirement allowance payments and who completed five years of creditable service if he became a member after July 1, 1979 or of a spouse receiving an accidental death benefit.
Amount	<p>Lump sum equal to one-half of the average final compensation on which the retirement allowance of the deceased retired member or spouse was based. The lump sum is payable to the surviving spouse, to unmarried children under age 18, or unmarried children over age 18 who are physically or mentally unable to make a living.</p> <p>In the case of a retired member who dies and leaves a surviving spouse, the spouse may elect to receive, in lieu of the lump sum death benefit, a monthly benefit payable until death or remarriage which is equal to one-half of the retirement allowance which the deceased member was receiving at the time of his death, provided the member had not made an optional election. If the spouse dies or remarries before the youngest unmarried child attains age 18, the pension will continue to the date that all the children have died, married or attained age 18, whichever occurs first. If the spouse was receiving payments on or before June 30, 1978, payments shall continue after remarriage with no further payments after death.</p>

Return of Contributions

Eligibility	Termination of membership prior to death.
Amount	If not eligible for a retirement allowance, all contributions with not less than one-half of interest credited. If eligible for normal or early service, ordinary disability, accidental disability or vested retirement allowance, his contributions, if any, with not less than one-half of the interest credited. The member may elect, prior to the commencement of his retirement allowance, to receive an annuity which is the actuarial equivalent of his accumulated contributions.

Summary of Plan Provisions (Concluded)

NORMAL AND OPTIONAL FORMS OF BENEFITS

Normal Life	Life Annuity
Option A	A reduced pension with the provision that at death, the reduced pension will be continued throughout the life of the designated beneficiary.
Option B	A reduced pension with the provision that at death, one-half of the reduced pension will be continued throughout the life of the designated beneficiary.
Option C	A reduced pension with the provision that at death, some other benefit approved by the Board will be payable.

CONTRIBUTIONS

By Members	No contributions are required.
By City	Annual contributions actuarially computed to be required to cover the cost of benefits of the System.

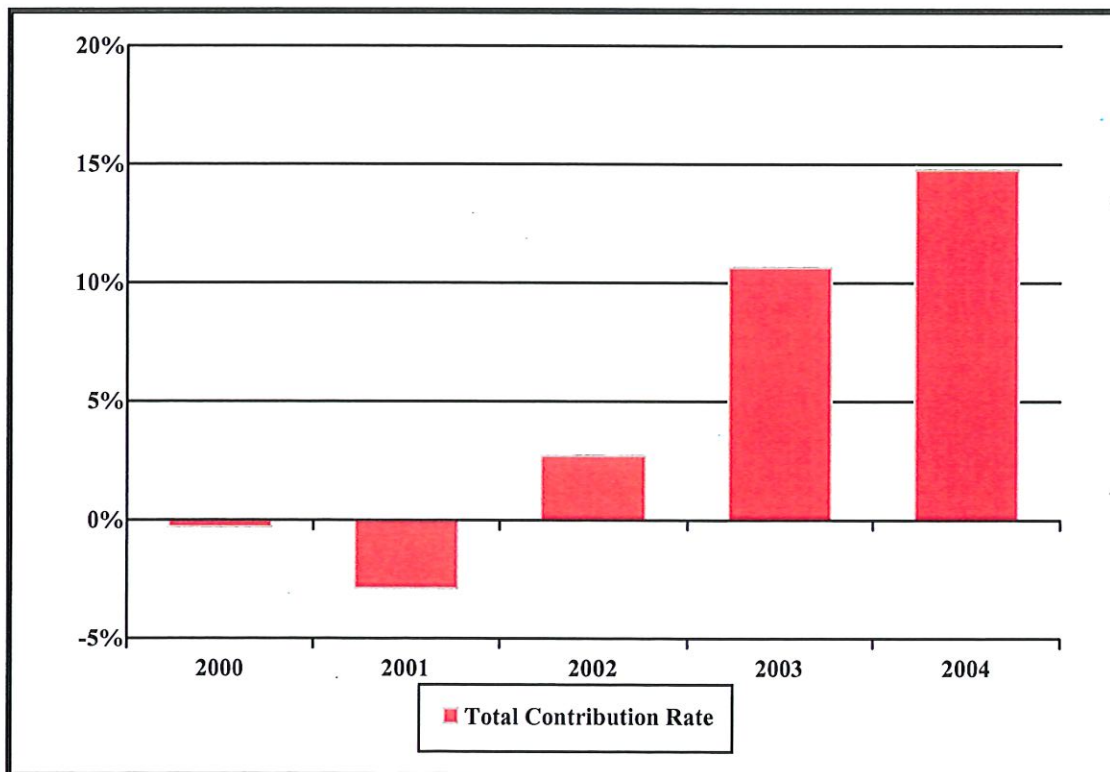
System Trends

Five-Year History of Contribution Rates (As a % of payroll)

Year Beginning July 1	Contribution Rate		
	Normal Cost	Unfunded Accrued Liability	Total
2004	13.03	1.74	14.77
2003	13.06	(2.41)	10.65
2002	13.09	(10.38)	2.71
2001	13.07	(15.96)	(2.89)
2000	13.02	(13.31)	(.29)

The following chart shows the System's five-year history of contribution rates:

Five-Year History of Contribution Rates



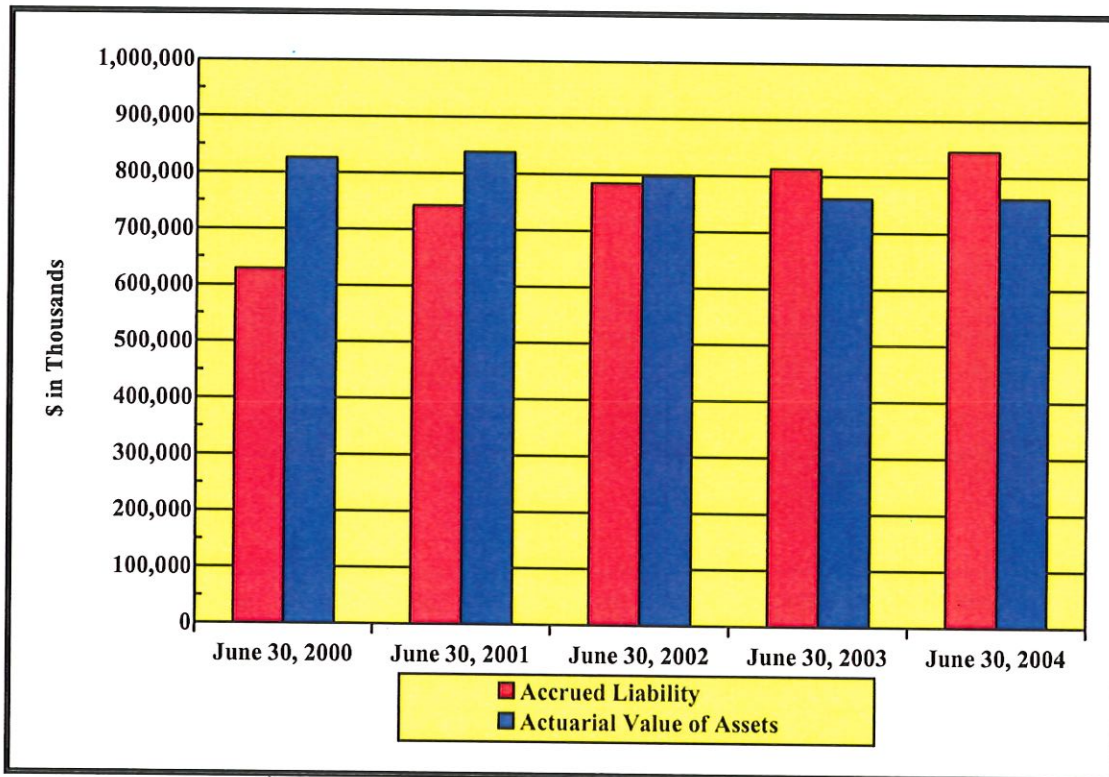
System Trends (Continued)

Five-Year History of Funded Ratio
(\$ results reported in thousands)

Valuation as of June 30	Accrued Liability	Actuarial Value of Assets	Unfunded Accrued Liability	Funded Ratio
2004	\$845,670	\$ 761,470	\$ 84,200	90.0%
2003	813,237	760,503	52,734	93.5
2002	784,652	798,071	(13,419)	101.7
2001	742,603	838,074	(95,471)	112.9
2000	628,252	826,439	(198,187)	131.5

The following chart shows the System's five-year history of the accrued liability and the actuarial value of assets:

Five-Year History of Accrued Liability and Actuarial Value of Assets



Statistical Section

STATISTICAL SECTION

**Active Employee Membership in Retirement System
as of June 30, 2004**

Group	Chapter 37	Total Membership
General Employees	2,644	2,644
Police Officers	730	730
Firefighters	437	437
Paramedics	43	43
City Council Members	7	7
Totals	3,861	3,861

**History of Active Employee Membership in Retirement System
Year Ended June 30**

Group	1998	1999	2000	2001	2002	2003	2004
General Employees	2,623	2,583	2,547	2,571	2,631	2,623	2,644
Police Officers	708	694	710	735	710	713	730
Firefighters	416	425	410	419	421	424	437
Paramedics	62	61	58	57	55	49	43
City Council Members	0	0	0	0	6	6	7
Totals	3,809	3,763	3,725	3,782	3,823	3,815	3,861

STATISTICAL SECTION

Retirement Granted During Fiscal Year 2004

Chapter 37	Service Retirements	Deferred Retirements	Disability	2004
General Employees and Lake Taylor Employees	85	12	21	118
Police Officers, Firefighters and Paramedics	40	8	10	58
Totals	125	20	31	176

History of Retirements Granted Year Ended June 30

Chapter 37	1998	1999	2000	2001	2002	2003	2004
Service Retirements	58	89	127	123	104	111	125
Deferred Retirements	13	17	16	19	23	32	20
Disability	26	33	16	17	18	24	31
Totals	97	139	159	159	145	167	176

**Summary of Annual Retirement Allowances
(Retirees and Survivors)
As of June 30, 2004**

Chapter 37	Service Retired Members		Contingent Annuitants		Disabled Annuitants		Total
	Counts	Amount	Counts	Amount	Counts	Amount	Counts
General Employees and Lake Taylor Employees	1,410	19,854,228	320	1,691,588	223	2,436,386	1,953
Police Officers, Firefighters and Paramedics *	526	13,826,054	157	1,229,582	146	2,632,420	829
Totals	1,936	33,680,282	477	2,921,170	369	5,068,806	2,782

* Council Members Included

STATISTICAL SECTION

History of Annual Retirement Allowances (In thousands of dollars) As of Year End June 30

Service Type	1998		1999		2000		2001		2002		2003		2004	
	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount
Service Retired Members	1,723	\$24,113	1,746	\$ 24,778	1,770	\$ 25,727	1,796	\$ 27,505	1,822	\$ 29,345	1,885	\$31,526	1,936	\$ 33,680
Contingent Annuitants	451	2,137	440	2,140	453	2,279	467	2,491	469	2,575	463	2,685	477	2,921
Disabled Annuitants	336	3,563	359	3,905	359	4,023	356	4,201	355	4,506	362	4,714	369	5,068
Totals	2,510	\$29,813	2,545	\$ 30,823	2,582	\$ 32,029	2,619	\$ 34,197	2,646	\$ 36,426	2,710	\$38,925	2,782	\$ 41,669

Income and Expenditures (In million dollars) Year Ended June 30

INCOME	1998	1999	2000	2001	2002	2003	2004
Contribution Payment	12.1	10.2	3.5	0.0	0.0	4.3	17.0
Interest and Dividend Income	24.9	25.0	26.5	27.9	21.2	17.1	15.0
Appreciation/(Depreciation)	96.0	53.6	47.9	-44.9	-79.3	24.2	69.9
Profit on sale of securities	49.6	69.0	63.4	86.4	33.3	35.3	80.7
Loss on sale of securities	-0.9	-9.6	-2.0	-59.2	-63.5	-55.2	-23.2
Unrealized Appreciation/(Depreciation)	47.3	-5.8	-13.5	-72.1	-49.1	44.1	12.4
TOTAL INCOME	133.0	88.8	77.9	-17.0	-58.1	45.6	101.9
EXPENDITURES							
Benefit Payments	28.8	29.9	31.0	32.0	35.3	36.9	39.5
Recurring Monthly Benefits from Pension Accum Acct	28.6	29.6	30.7	31.8	35.0	36.7	39.4
Refunds or Cashouts from Annuity Savings Acct	0.1	0.1	0.1	0.1	0.1	0.1	0.0
Lump Sum Death Benefits from Pension Accum Acct	0.1	0.2	0.2	0.1	0.2	0.1	0.1
Expenses	2.8	2.4	2.6	3.2	3.3	3.0	2.9
Investment (or "Professional")	2.5	2.0	2.1	2.9	3.0	2.2	2.5
Administrative	0.3	0.4	0.5	0.3	0.3	0.8	0.4
TOTAL EXPENDITURES	31.6	32.3	33.6	35.2	38.6	39.9	42.4

STATISTICAL SECTION

Plan Net Assets (In million dollars) Year Ended June 30

	1998	1999	2000	2001	2002	2003	2004
Fund Balance, BOY (At Market)*	674.1	775.5	832.0	876.3	824.1	727.4	733.2
Income	133.0	88.8	77.9	(17.0)	(58.1)	45.6	101.9
Expenses	31.6	32.3	33.6	35.2	38.6	39.9	42.4
Net Income	101.4	56.5	44.3	(52.2)	(96.7)	5.7	59.5
Fund Balance, EOY *	775.5	832.0	876.3	824.1	727.4	733.1	792.7

*Excludes receivable
contributions

Payment Receivable	10.1	3.5	0.0	0.0	4.3	17.0	23.5
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Participant and Investment Data and Ratio Year Ended June 30

	1998	1999	2000	2001	2002	2003	2004
Participant Data:							
Active Employees (EOY) *	3,809	3,763	3,725	3,782	3,823	3,815	3,861
Retirees and Beneficiaries (EOY)	2,510	2,545	2,582	2,619	2,646	2,710	2,782
Retirees as a % of Actives	65.9%	67.6%	69.3%	69.2%	69.2%	71.0%	72.1%
Retirement Benefits Paid (\$ in Millions)	29.8	30.8	32.0	34.2	36.4	38.9	41.7
Average Benefit Payment (\$/Month)	\$990	\$1,009	\$1,034	\$1,088	\$1,147	\$1,197	\$1,248
Investment Data:							
Fund Balance (Market Value)	775.5	832	876.3	824.1	727.4	733.1	792.7
Ratio: Fund Balance / Benefits Paid	26.0	27.0	27.4	24.1	20.0	18.8	19.0

* Layoffs not included

STATISTICAL SECTION

**Contribution Analysis
(In million dollars)
Year Ended June 30**

	1998	1999	2000	2001	2002	2003
Estimated Covered Payroll	122.2	129	129.9	144.2	150.7	152.1
Contribution Rate						
Normal Cost Rate	13.12%	13.02%	13.07%	13.09%	13.06%	13.03%
Amortization Rate	-10.42%	-13.31%	15.96%	-7.58%	-2.41%	1.74%
Total	2.70%	-0.29%	-2.89%	5.51%	10.65%	14.77%
Accrued Liabilities	569.9	601.4	628.3	742.6	784.7	813.2
Market Value of Assets with receivable	785.6	835.5	876.3	824.1	731.7	750.1
Funded Ratio	137.8%	138.9%	139.5%	111.0%	93.2%	92.2%
Actuarial Value of Assets	694.2	767.8	826.4	838.1	798.1	760.5
Funded Ratio	121.8%	127.7%	131.5%	112.9%	101.7%	93.5%

The information presented above was determined as part of the actuarial valuation as of one year prior to the dates indicated (i.e., the contribution determined by the valuation completed as of June 30, 2003 was accrued and payable for the fiscal year ending June 30, 2004).

Norfolk Employees' Retirement System
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