

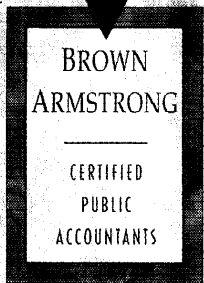
**PASADENA FIRE AND POLICE RETIREMENT SYSTEM
A PENSION TRUST FUND OF THE CITY OF
PASADENA, CALIFORNIA**

**REPORT AND AUDITED FINANCIAL STATEMENTS
WITH REQUIRED SUPPLEMENTAL INFORMATION**

FOR THE YEARS ENDED JUNE 30, 2006 AND 2005

**PASADENA FIRE AND POLICE RETIREMENT SYSTEM
FOR THE YEARS ENDED JUNE 30, 2006 AND 2005
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BROWN ARMSTRONG
PAULDEN McCOWN STARBUCK THORNBURGH & KEETER
CERTIFIED PUBLIC ACCOUNTANTS

Main Office
4200 Truxtun Ave., Suite 300
Bakersfield, California 93309
Tel 661-324-4971 Fax 661-324-4997
e-mail: info@bacpas.com

Shafter Office
560 Central Avenue
Shafter, California 93263
Tel 661-746-2145 Fax 661-746-1218

- Andrew J. Paulden, CPA
Peter C. Brown, CPA
Burton H. Armstrong, CPA, MST
Harvey J. McCown, MBA, CPA
Steven R. Starbuck, CPA
Aileen K. Keeter, CPA
Chris M. Thornburgh, CPA
Eric H. Xin, MBA, CPA
Lynn R. Krausse, CPA, MST
Bradley M. Hankins, CPA
Rosalva Flores, CPA
Connie M. Perez, CPA
M. Sharon Jones, CPA, MST
Diana H. Branthoover, CPA
Matthew R. Gilligan, CPA
Michael C. Olivares, CPA
Hanna J. Sheppard, CPA
Ryan S. Johnson, CPA

INDEPENDENT AUDITOR'S REPORT

To the Retirement Board
Pasadena Fire and Police Retirement System

We have audited the accompanying statement of plan net assets of the Pasadena Fire and Police Retirement System (the "System") as of June 30, 2006 and the related statement of changes in plan net assets for the year then ended. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Pasadena Fire and Police Retirement System as of and for the year ended June 30, 2005 were audited by other auditors, whose report dated December 9, 2005, expressed an unqualified opinion on those statements.

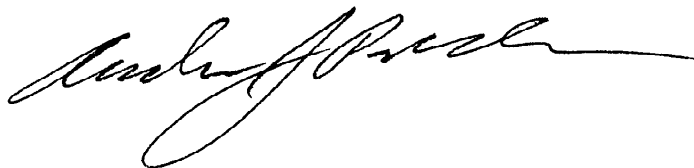
We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net assets of the Pasadena Fire and Police Retirement System as of June 30, 2006 and the changes in plan net assets for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis as listed in the table of contents is 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 this required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The information designated as other supplementary information in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements of the System. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

BROWN ARMSTRONG PAULDEN
McCOWN STARBUCK THORNBURGH & KEETER
ACCOUNTANCY CORPORATION



Bakersfield, California
August 31, 2006

Pasadena Fire and Police Retirement System Management's Discussion and Analysis (MD&A) (Unaudited)

The Pasadena Fire and Police Retirement System ("System", or "Plan") is a defined benefit Plan governed by a Retirement Board ("Board") under provisions of the City of Pasadena ("City") Charter. The System was closed to new members on June 30, 1977, but continues to pay out benefits to retirees and their beneficiaries. The System covers all fire and police personnel who were employed by the City prior to July 1, 1977, except those who elected to transfer to the California Public Employees Retirement System ("CalPERS") either when the System closed to new members or in June 2004. In June 2004 active members were provided a one-time opportunity to transfer from the System to CalPERS as provided for by an agreement with the City and CalPERS. Ten members elected to move to CalPERS. The Board is comprised of one member of the City Council, two Pasadena residents appointed by the City Council, and two active members of the Retirement System elected under the supervision of the Retirement System. Board members are elected to terms of four years with no restriction on reappointment.

Our discussion and analysis of the System's financial performance presents an overview of the System's financial activities during the fiscal years ended June 30, 2006 and 2005. This discussion and analysis should be read in conjunction with and is qualified in its entirety by the accompanying audited financial statements and footnotes which begin following this MD&A. The financial statements, footnotes and this discussion and analysis were prepared by management and are the responsibility of management.

Financial Highlights

During the fiscal year ended June 30, 2006, the System continued to benefit from the strong performance of the financial markets as evidenced by the following.

The Change in Plan Net Assets Held in Trust for Pension Benefits increased by \$773,000 from the prior year. This compares with a decrease of \$908,000 in the prior year. This was due to the good return on investments and the one time contribution of \$1,407,378 from the Settlement and Release Agreement No. 18,550 ("Settlement Agreement") (Note 6) that was recognized in fiscal year 2006.

Due to the strong performance in many of the financial markets, especially with the equity and real estate markets, net investment gains for the Plan were \$13,713,000 as compared to net investment gains of \$13,178,000 in the prior fiscal year. The current fiscal year investment gains were consistent with the overall market conditions.

Contributions increased by \$1,373,000 and for the fiscal year were \$1,484,000. The current year contributions consisted primarily of \$1,407,378 of contributions that were received from the City under the Contribution Agreement. The remaining contributions consisted of active members cost-of-living contributions of 5% of covered salary that is matched 100% by the City and employee contributions of 9% of covered salary for both fire and police personnel made by the City on behalf of the employee and credited to their individual accounts.

Deductions from the Net Assets primarily consisted of the payment of benefits to members and their beneficiaries and the costs of administering the Plan. These deductions increased to \$14,190,000 in the current fiscal year. This represented a \$221,488 or 1.6% increase compared to the prior year and was due to increased benefit payments resulting from the annual cost of living adjustment and the addition of two new retired members. The increase was only partially offset by the deaths of other members.

Pasadena Fire and Police Retirement System Management's Discussion and Analysis (MD&A) (Unaudited)

The System engaged Public Pension Professionals to serve as its independent actuary. The most recent actuarial valuation was prepared as of June 30, 2006 and determined the funded percentage to be 69.1% as compared to 71.7% in the prior year. The decrease was primarily attributed to the normal operation of the plan and the continued spreading of previous losses into the current year. The market asset rate of return of 10.4% exceeded the assumed rate of 8%.

As provided by Contribution Agreement No.16,900 ("Contribution Agreement"), if the funded percentage is below the minimum funding percentage of 73% for FY 2006, the City will reimburse the System in the following fiscal year subject to certain reimbursement limits. Based on the June 30, 2006 actuarial valuation the minimum funding deficit was \$7,160,798 or 3.87% to meet the funding requirement of 73%, as of June 30, 2006. This compared to a minimum funding deficit of \$1,407,378 to meet the minimum funding requirement of 72.5% as of June 30, 2005. The Contribution Agreement states that if this minimum funding deficit is greater than \$3,000,000 the City will pay \$3,000,000 to the System and any remaining amount necessary to reach the minimum funding percentage is phased in over a five-year period. Based on these provisions the required supplemental contribution by the City was \$3,832,160 and is due to the System no later than January 2, 2007.

Overview of Financial Statements

This Management's Discussion and Analysis serves as an introduction to the basic financial statements. The System has two basic financial statements, the notes to the financial statements, and required supplementary schedules of actuarial information. The basic financial statements and required disclosures are in compliance with the accounting principles and reporting guidelines as set forth by the Governmental Accounting Standards Board, utilizing the accrual basis of accounting.

The first financial report is the Statement of Plan Net Assets and represents the balances at fiscal year end. The net assets, which are the assets less the liabilities, represent the funds available for future use in the payment of benefits and administration of the Plan.

The second statement is the Statement of Changes in Plan Net Assets which reflects the activity during the fiscal year and shows the effect of the additions and deductions to the Plan.

Condensed Statement of Plan Net Assets

	<u>June 30,</u>	
	<u>2006</u>	<u>2005</u>
	(In Thousands)	
Current Assets	\$ 1,432	\$ 6,647
Investments	<u>135,145</u>	<u>129,130</u>
Total Assets	136,577	135,777
Total Liabilities	<u>145</u>	<u>118</u>
Total Plan Net Assets	<u>\$ 136,432</u>	<u>\$ 135,659</u>

**Pasadena Fire and Police Retirement System
Management's Discussion and Analysis (MD&A) (Unaudited)**

As of June 30, 2006, the System had \$136,432,000 in Net Assets. The Net Assets represent funds available for future payments. However, public pension funds are not required to disclose the future obligations owed to retirees. Only current liabilities are reported on the Statement of Plan Net Assets.

Condensed Statement of Changes in Plan Net Assets

	<u>June 30,</u>	
	<u>2006</u>	<u>2005</u>
	(In Thousands)	
Employer Contributions	\$ 1,427	\$ 29
Employee Contributions	57	82
Investment Gain	<u>13,713</u>	<u>13,178</u>
Total Additions	15,197	13,289
Benefit Payments	14,190	13,969
Administrative Expenses	<u>234</u>	<u>228</u>
Total Deductions	<u>14,424</u>	<u>14,197</u>
Net (Decrease) Increase	<u>\$ 773</u>	<u>\$ (908)</u>

During the year ended June 30, 2006, Plan Net Assets increased by \$773,000, primarily as a result of changing market conditions in the current year and the one time contribution of \$1,407,378 from the Settlement Agreement.

**PASADENA FIRE AND POLICE RETIREMENT SYSTEM
STATEMENTS OF PLAN NET ASSETS
JUNE 30, 2006 AND 2005**

	June 30,	
	2006	2005
	(In Thousands)	
Assets		
Cash	\$ 1,084	\$ 6,307
Accrued Interest Receivable	348	340
Investments, at fair value		
U.S. Government obligations	18,148	12,736
Domestic corporate bonds	17,453	21,263
International corporate bonds	775	1,358
Real estate (REITS)	18,836	16,878
International stock	17,008	14,423
Domestic stock	62,925	62,472
Total Investments, at fair value	135,145	129,130
Total Assets	136,577	135,777
Liabilities		
Accounts payable	145	118
Total Liabilities	145	118
Net assets held in trust for pension benefits (a schedule of funding progress is presented in the required supplemental information)	\$ 136,432	\$ 135,659

The accompanying notes are an integral part of these financial statements.

**PASADENA FIRE AND POLICE RETIREMENT SYSTEM
STATEMENTS OF CHANGES IN PLAN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2006 AND 2005**

	June 30,	
	2006	2005
(In Thousands)		
Additions		
Contributions		
City	\$ 1,427	\$ 29
Plan members	57	82
Total Contributions	1,484	111
Investment Income		
Net appreciation in fair market value of investments	11,287	10,694
Interest	2,133	1,920
Dividends	978	1,021
Net investing activity income	14,398	13,635
Less investment expenses	(685)	(457)
Total net investment income	13,713	13,178
Total additions	15,197	13,289
Deductions		
Benefits paid to participants	14,190	13,969
Administrative expenses	234	228
Total Deductions	14,424	14,197
Net (Decrease) Increase	773	(908)
Net Assets Held in Trust for Pension Benefits		
Beginning of Year	135,659	136,567
End of Year	\$ 136,432	\$ 135,659

The accompanying notes are an integral part of these financial statements.

**PASADENA FIRE AND POLICE RETIREMENT SYSTEM
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2006**

NOTE 1 – DESCRIPTION OF THE PLAN

General

The Pasadena Fire and Police Retirement System ("System") is a defined benefit Plan governed by a Retirement Board ("Board") under provisions of the City of Pasadena ("City") Charter. The Plan covers all fire and police personnel who were employed by the City prior to July 1, 1977, except for those who elected to transfer to the California Public Employees Retirement System ("CalPERS") when the System closed to new members or in June 2004. In June 2004 active members were provided a one-time opportunity to transfer from the System to CalPERS as provided by an agreement with the City. Once transferred to CalPERS retirement benefits for all fire and police personnel employed thereafter are provided under CalPERS.

The System is a single-employer public employees' retirement System which is included as a pension trust fund in the financial statements of the City of Pasadena, California.

As of June 30, 2006, there were 314 retirees and beneficiaries currently receiving benefits and 1 active employee, who is fully vested in the Plan. As of June 30, 2005, there were 322 retirees and beneficiaries currently receiving benefits and 3 active employees.

Benefit provisions are established and may be amended by the City Charter.

Pension Benefits

Members are entitled to annual pension benefits beginning at normal retirement age (50) equal to 1/50 of final compensation multiplied by an actuarial equivalent based on the actual retirement age. The Plan permits service retirement at age 50, provided at least 15 years of service have been rendered, or retirement after 25 years of service, regardless of age.

Disability Benefits

Generally, active members who become totally disabled receive annual disability benefits that are equal to 50% of final compensation.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The System follows the accounting principles and reporting guidelines as set forth in Statement No. 25 of the Governmental Accounting Standards Board ("GASB"). The financial statements are prepared using the accrual basis of accounting. Member and employer contributions are recognized in the period in which the contributions are due and when the City has made a formal commitment to provide the contributions. Benefits are recognized when payable, in accordance with the terms of the Plan.

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 certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Reclassifications

Comparative data for the prior year has been presented in the selected sections of the accompanying Statements of Plan Net Assets and Changes in Plan Net Assets. Also, certain accounts presented in the prior year's data may have been reclassified in order to be consistent with the current year's presentation.

NOTE 3 – INVESTMENTS

Investments are reported at fair market value. The System determined the market value of publicly traded securities based upon the published closing price of the security on June 30, 2006 and 2005.

Authorized Investments

In conformance with its Charter, the Retirement Board shall have the sole power and authority under such general ordinances as may be adopted by the legislative body to hear and determine all facts pertaining to applications for and awards of any benefits under the System, or any matters pertaining to the administration thereof. The Retirement Board shall have exclusive control of the administration and investment of such fund or funds as may be established and all investments shall be subject to the same terms, limitations and restrictions as are imposed by the Constitution and laws of the State upon the investment of the CalPERS Funds, as now enacted or hereafter amended.

Pursuant to this authority, the Retirement Board has authorized investment in the following securities:

- Securities of the U.S. Government or its agencies
- Certificates of Deposit, or Time Deposits, placed with commercial banks and savings and loan associations
- Negotiable Certificates of Deposit
- Banker's acceptances
- Commercial paper (rated A-1/P-1 or better)
- Medium-Term Corporate Notes (up to five years maturity)
- Corporate and Municipal Bonds
- Preferred stock
- Common stock
- Fixed-income funds
- Foreign stock and corporate bonds
- Mutual funds
- Real Estate Investment Trust (REIT)

Credit Risk and Market Value of Investments

The Board has the exclusive control over the System's investment portfolio as prescribed by Article XV, Section 1502 of the City of Pasadena Charter. The Board has established the Investment Objectives, Guidelines and Standards of Performance in accordance with applicable local, State, and Federal laws. The Board members exercise authority and control over the management of FPRS's assets (the Plan) by setting policy which the Board executes through the use of external prudent experts. The Board oversees and guides the Plan subject to the following basic fiduciary responsibilities:

- Solely in the interest of, and for the exclusive purpose of, providing economic benefits to participants and their beneficiaries.
- With the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character with like objectives.

NOTE 3 – INVESTMENTS (Continued)

Credit Risk and Market Value of Investments (Continued)

- Diversify the investments of the Plan so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances, it is clearly prudent not to do so. Diversification is applicable to the deployment of the assets as a whole.

The Investment Guidelines encompasses the following:

- Domestic Fixed Income Guidelines
- Domestic Equity Guidelines
- International Equity Guidelines
- Real Estate Investment Trust Guidelines

Credit Risk

Credit Risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The System seeks to maintain a diversified portfolio of fixed income instruments in order to obtain the highest total return for the fund at an acceptable level of risk within this asset class. The credit quality ratings of investments in fixed income securities by a nationally recognized statistical rating organization, the S & P, as of June 30, 2006 are as follows:

Credit Quality Ratings of Investments in Fixed Income Securities

<u>Quality Ratings - S & P</u>	<u>Fair Value</u>	<u>Percentage</u>
AAA	\$ 18,176,840	49.97%
A	2,578,954	7.09%
BBB	4,054,232	11.15%
BB	427,594	1.18%
B	829,503	2.28%
Not Rated	3,254,885	8.95%
Rating Not Determined	7,054,409	19.39%
	<u>\$ 36,376,417</u>	<u>100.00%</u>

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of a financial institution's failure, the System would not be able to recover its deposits or would not be able to recover collateral securities that are in the possession of an outside party. Deposits are exposed to custodial credit risk if they are not insured or not collateralized. As of June 30, 2006, the System is not exposed to such risk on the fair value of total international investments. The System's policy requires the international investment managers to hold no more than 7% of their portfolios in the form of cash.

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the System would not be able to recover the value of the 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 not insured, or are not registered in the System's name, and held by the counterparty. The System's investments are not exposed to custodial credit risk if they are insured or registered in the System's name. The System's investments are not exposed to custodial credit risk since all securities are held by the System's custodial bank in the System's name.

NOTE 3 – INVESTMENTS (Continued)

Concentration of Credit Risk

As of June 30, 2006, the FPRS portfolio did not hold any investments in any one issuer that would represent five percent (5%) or more of total investments. Investments issued or explicitly guaranteed by the U.S. Government and pooled investments are excluded from this requirement.

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Duration is a measure of the price sensitivity of a fixed income portfolio to changes in interest rates. It is calculated as the weighted average time to receive a bond's coupon and principal payments. The longer the duration of a portfolio, the greater its price sensitivity is to changes in interest rates.

One of the ways the System manages its exposure to interest rate risk is by requiring the fixed income investment managers to maintain their portfolio effective duration within a specified range of the Lehman U.S. Universal Bond Index, the Lehman Intermediate Government Credit Index, or the Lehman Aggregate Bond Index, depending on the Board's mandates. The effective duration is a measure, in years, of interest-rate sensitivity in debt investments. The longer the effective duration, the greater the sensitivity to interest rate changes.

Information about the sensitivity of the fair values of the System's investments to market interest rate fluctuations is provided by the following table that shows the weighted average effective duration of the System's fixed income investments by investment type:

Fixed Income Securities		
As of June 30, 2006		
<u>Investment Type</u>	<u>Fair Value</u>	<u>Duration</u>
U.S. Government and Agency Instruments		
Government Bonds	\$ 11,809,444	4.96
Government Mortgage Backed Securities	6,338,781	5.74
Total	18,148,225	
Corporate Securities		
Corporate Bonds	6,919,110	5.07
Non-Government Backed C.M.O.'s	5,288,219	4.02
Asset Backed Securities	2,138,655	4.55
Commercial Mortgage Backed Securities	3,107,336	4.62
Total	17,453,320	
International Fixed Income	774,872	3.88
Total Fixed Income Securities	\$ 36,376,417	4.46

NOTE 3 – INVESTMENTS (Continued)Highly Sensitive Investments

Highly Sensitive Investments are certain debt investments whose terms may cause their fair value to be highly sensitive to market interest rate changes. Terms include such information as embedded options, coupon multipliers, benchmark indexes, and reset dates. The System's asset-backed investments have embedded prepayment options that will typically cause prepayments by the obligees of the underlying investments when interest rates fall. Prepayments eliminate the stream of future interest payments and, therefore, diminish the fair value of the asset-backed investment. The following table shows the fair value of the System's asset-backed investments by investment type:

<u>Investment Type</u>	<u>Amount</u>
Government Mortgage Backed Securities	\$ 6,338,781
Asset Backed Securities	2,138,655
Commercial Mortgage Backed Securities	3,107,336
Non-Government Backed Commercial Mortgage Obligations	5,288,219
Total	<u>\$ 16,872,991</u>

Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or deposit. The System's asset allocation policy sets a target of 10% of the total portfolio for non-U.S. investments in equities. Currency hedging will be permitted as part of a defensive strategy to protect the portfolio's underlying assets.

The System's non-U.S. investment holdings as of June 30, 2006 are as follows:

<u>Foreign Currency Type</u>	<u>Fair Value in USD</u>
Australian Dollar	\$ 319,860
Swiss Franc	898
United Kingdom	454,114
Total International Investments	<u>\$ 774,872</u>

Cash and Investments

Cash and investments as of June 30 were held as follows:

	<u>June 30,</u>	
	<u>2006</u>	<u>2005</u>
	<u>(In Thousands)</u>	
Cash in Bank - Held by Trustee and the City	\$ 1,084	\$ 6,307
Investments - Held by Trustee	135,145	129,130
	<u>\$ 136,229</u>	<u>\$ 135,437</u>

NOTE 4 – CONTRIBUTION INFORMATION

Contribution requirements are established and, subject to any constitutional limitations, may be amended by the City Charter.

General

Historically the City has made monthly contributions to the System based on actuarially determined employer contribution rates which, together with employee contributions, were expected to provide sufficient assets to pay funded basic benefits when due. However, the Charter did not require actuarially determined funding for unfunded basic, 1919, and COLA benefits, which are funded under Contribution Agreement #16,900, dated March 18, 1999 between the City and the Retirement System. Per the terms negotiated through their respective recognized Associations, employee contributions of 9% for both fire and police personnel base earnings were made by the City on behalf of the employee and credited to their individual accounts.

Member Contributions

As a condition of participation, members were required to contribute the following percentage of their annual salary to the Plan:

<u>Age of Entry Into the Plan</u>	<u>Percent of Annual Salary Contributed</u>
21	9.10
22	9.19
23	9.29
24	9.38
25	9.48
26	9.57
27	9.67
28	9.77
29	9.87
30	9.96
31	10.06
32	10.16
33	10.27
34	10.37
35	10.47

The funding Plan was updated on March 18, 1999 when the System entered into Contribution Agreement No. 16,900 with the City of Pasadena. As a result of this agreement, the City of Pasadena made a contribution of \$100,000,000 to the System on August 5, 1999. Per the Contribution Agreement, the System is considered to meet minimum funding requirements for the year ended June 30, 2001 if the funded percentage exceeds 70%. The minimum funded percentage will increase by 1/2% each year until it reaches 80% in the year ending June 30, 2020. Thereafter it may, but need not, be changed by the System.

Based on the Contribution Agreement, the City discontinued its 9% contribution to the Fire and Police Retirement System on behalf of these employees, as the City considered these contributions fully funded. These contributions terminated on August 1, 1999 through April 5, 2001.

During May and June of 2000 the Pasadena Police Officers Association, Pasadena Police Sergeants Association, the Pasadena Firefighters Management Association, and the Pasadena Fire Fighters Association filed grievances to have these contributions reinstated. As a result these contributions were reinstated and will continue indefinitely regardless of the funding status of the Plan. In addition the 9% contributions were retroactively credited with interest for the period of August 1, 1999 through April 4, 2001. These retroactive contributions were \$207,000 and \$249,000 respectively, for 2001 and 2000.

NOTE 4 – CONTRIBUTION INFORMATION (Continued)

Active members are also required to make cost-of-living contributions as a percent of covered salary which amounted to 5% for 2006 and 2005, and which is matched 100% by the City. These contributions are made as long as the funding percentage is less than 100%.

The City Charter requires members' contributions to be credited to the individual account of the member from whose compensation the contribution was deducted. Such contributions accrue interest at a rate determined by the Retirement Board and are either to be refunded to members or their beneficiaries upon separation from City service for reasons other than retirement, or to be applied towards providing members' retirement or death allowances. Amendments to the City Charter cannot prevent the refund of such contributions plus accrued interest. Active members' accumulated contributions at June 30, 2006 and 2005 were \$614,406 and \$1,730,241, respectively, including interest credited at a rate of 8% for 2006 and 2005.

NOTE 5 – ADMINISTRATIVE COSTS

The administrative costs to administer the Plan are paid by the System.

NOTE 6 – SUPPLEMENTAL FUNDING PLAN

The Plan engages an independent actuary to perform an annual actuarial valuation. The results of the valuation as of June 30, 2006 are presented in the Schedule of Funding Progress, which includes historical trend information about the actuarially determined funded status of the Plan from a long-term, ongoing Plan perspective and the progress made in accumulating sufficient assets to pay benefits when due, and Schedule of Employer Contributions.

The latest annual valuation was performed as of June 30, 2006. The System uses the entry age normal actuarial cost method, which is a projected benefit cost method (that is, it takes into account those benefits that are expected to be earned in the future as well as those already accrued).

According to this cost method, the normal cost for an employee is the level amount which would fund the projected benefit if it were paid annually from date of employment until retirement.

However, because of inadequate funding of cost-of-living benefits as well as changes through the years in the benefit structure and the actuarial assumptions, and because actuarial gains and losses caused by experience are different from such assumptions, an unfunded actuarial liability had developed.

To fund the unfunded actuarial liability, on November 21, 1989, the Board of Directors of the City of Pasadena approved in concept the assignment of assets to the System. On June 12, 1990, the Board of Directors adopted Resolution No. 6379, which formally assigned the recommended assets to the System in a formal "Contribution Agreement". The funding Plan is evaluated annually based on economic conditions and actuarial assumptions.

The funding Plan was updated on March 18, 1999 when the System entered into Contribution Agreement No. 16,900 with the City of Pasadena. As a result of this agreement, the City of Pasadena made a contribution of \$100,000,000 to the System on August 5, 1999.

During the year ended June 30, 2001, no additional supplemental contribution was made as Contribution Agreement No. 16,900 ("Contribution Agreement") states that no additional supplemental contributions are due if the aggregate funding percentage exceeded the minimum funding percentage of 70% for the year ended June 30, 2001, which is increased by one-half of one percent for each of the next 20 years.

NOTE 6 – SUPPLEMENTAL FUNDING PLAN (Continued)

As of June 30, 2006 and 2005, the actuarially determined unfunded accrued liability was \$57,010,803 and \$52,451,371 and the funded status of the System was 69.1% and 71.7% respectively. The funded status for 2006 and 2005 was below the required minimum funding percentages of 73% and 72.5%, respectively. The Contribution Agreement states that if the System falls below the minimum funding percentage the City will reimburse the System in the following fiscal year up to the amount necessary to restore the System to the minimum funding percentage as of the last day of the preceding fiscal year. The supplemental contributions in each year are subject to certain limitations as provided by the Contribution Agreement.

The minimum funding deficits were \$7,160,798 and \$1,407,378 as of June 30, 2006 and 2005 respectively. The Contribution Agreement states that if this minimum funding deficit is greater than \$3,000,000, the City will pay \$3,000,000 to the System and any remaining amount necessary to reach the minimum funding percentage is to be phased in over a five-year period. The required supplemental contributions by the City as of June 30, 2006 and 2005 were \$3,832,160 and \$1,407,378, respectively. As provided by the Contribution Agreement the contribution is due to the System in the subsequent fiscal year.

NOTE 7 – SETTLEMENT AGREEMENT

In October 2002, the Retirement Board accepted the Actuarial Valuation Report, dated June 30, 2002, including the adoption of a 20% corridor concept in the asset smoothing method. The corridor concept set a 20% corridor around the market value of the assets that the actuarial value of the assets is required to stay within to ensure that the actuarial value of the assets does not vary significantly from the market value. This method resulted in a minimum funding deficit of \$11,828,000 and a City contribution under the Contribution Agreement of \$4,766,000 that would be due in the subsequent fiscal year. However, the City disputed the use of the corridor concept and in January 2003 engaged an actuary to provide an opinion as to the appropriateness of the corridor concept. Excluding the use of the corridor concept the City calculated the minimum funding deficit to be \$80,000. This amount was contributed to the System in January 2003.

During 2003, the System filed a claim against the City for payment of the larger amount of the above contribution. This claim was deemed denied by the non-response by the City. In November 2003, the Retirement Board accepted the Actuarial Valuation Report, dated June 30, 2003, which utilized the 20% corridor concept in the asset smoothing method. This method resulted in a minimum funding deficit of \$20,296,000 and a City contribution under the Contribution Agreement of \$8,143,000 that would be due in January 2004.

In June 2004 the City and the System entered into Settlement and Release Agreement No. 18,550 ("Settlement Agreement") to settle the disputed use of the corridor method and the payment of the supplemental contributions. Under the terms of the Settlement Agreement the City made contributions of \$15,000,000, \$15,000,000, and \$10,000,000 in August 2004, October 2004, and December 2004 respectively. In addition a debenture was issued by the City in June 2004 for \$13,736,000 and the debenture was to be funded by the contributions provided for by the Settlement Agreement. Contribution amounts in excess of the debenture were applied to the supplemental contribution that was due to the System in January 2005. In consideration the System agreed to eliminate the use of the corridor concept methodology in all actuarial valuations on or subsequent to June 30, 2005. As of June 30, 2005 \$40,000,000 was collected by the Plan.

In October 2005, the Retirement Board accepted the Actuarial Valuation Report, dated June 30, 2005. The valuation included the \$40,000,000 of contributions received by the System under the Settlement Agreement, and allocated the \$13,736,000 used to repay the debenture issued in June 2004 as a contribution and asset as of June 30, 2004 based upon the provisions of the Settlement Agreement. The debenture of \$13,736,000 replaced earlier debentures issued by the City for Supplemental Contributions under Contribution Agreement #16,900. The payments under the Settlement Agreement in excess of the amount allocated to the debenture and included in the Plan assets in the prior year were included in Plan assets as of June 30, 2005.

NOTE 8 – TRANSFER OF MEMBERS TO CALPERS

In June 2004 active members were provided a one-time opportunity to transfer from the System to CalPERS as provided by an agreement with the City and CalPERS. Ten members elected this to transfer and in July 2004 assets of \$4,687,000 attributable to these members was transferred. These were recognized as payables in FY 2004.

NOTE 9 – COMMITMENTS AND CONTINGENCIES

The City of Pasadena Board of Directors adopted Resolution 6179 at its July 18, 1989 meeting assigning a 93% beneficial interest in the Concord property at 275 E. Cordova, Pasadena, to the Pasadena Fire and Police Retirement System. The property is currently used for federally subsidized housing and it is subject to federal restrictions on its use. Because of uncertainties surrounding the permitted future use of this property by the City, the System's interest in this asset is carried at a zero value.

NOTE 10 – REQUIRED SUPPLEMENTARY INFORMATION

The schedule of the system's funding progress against the actuarial accrued liability and the schedule of required employer Annual Required Contribution (ARC) and the percentage of the ARC recognized by the Plan are presented, where available, on the following pages as Required Supplementary Information.

REQUIRED SUPPLEMENTAL INFORMATION

**PASADENA FIRE AND POLICE RETIREMENT SYSTEM
SCHEDULE OF FUNDING PROGRESS
(AMOUNTS IN THOUSANDS)
JUNE 30, 2006**

Actuarial Valuation Date	(a) Actuarial Value of Plan Assets	(b) Actuarial Accrued Liability (AAL)	(b-a) Unfunded AAL	(a/b) Funded Ratio	(c) Annual Covered Payroll	UAAL as a % of Covered Payroll
June 30, 2006	\$ 127,841	\$ 184,852	\$ 57,011	69%	\$ 141	40,416 %
June 30, 2005	132,730	185,181	52,451	72%	278	18,902 %
June 30, 2004 *	117,100	186,072	68,972	63%	380	18,167 %
June 30, 2003	122,105	199,168	77,063	61%	2,248	3,428 %
June 30, 2002 **	128,325	197,448	69,123	65%	2,697	2,563 %
June 30, 2001 ***	152,700	192,615	39,915	79%	2,976	1,341 %
June 30, 2000	159,718	184,173	24,445	87%	3,016	811 %
June 30, 1999	68,194	213,183	144,988	32%	3,113	4,657 %
June 30, 1998	63,992	214,232	150,240	30%	3,314	4,534 %
June 30, 1997	61,190	218,577	157,387	28%	3,562	4,418 %

* The actuarial value of Plan assets does not include the contribution receivable due under the Settlement Agreement, but does include a receivable for the debenture issued in June 2004 (see Note 7).

** The change in the funded status between June 30, 2001 and June 30, 2002 was affected by changes in benefits assumptions and a refinement of actuarial asset valuation methods.

*** The change in the funded status between June 30, 2000 and June 30, 2001 was affected by changes in benefits and actuarial assumptions.

**PASADENA FIRE AND POLICE RETIREMENT SYSTEM
 SCHEDULE OF EMPLOYER CONTRIBUTIONS
 (AMOUNTS IN THOUSANDS)
 JUNE 30, 2006**

<u>Fiscal Year Ended</u>	<u>Annual Required Contribution</u>	<u>Actual Contribution</u>	<u>Percentage of ARC Recognized as Contribution</u>
June 30, 2006	\$ 12,674	\$ 1,427	11%
June 30, 2005	16,665	26,293	158%
June 30, 2004	24,425	13,863	57%
June 30, 2003	16,972	212	1%
June 30, 2002	8,688	148	2%
June 30, 2001	5,326	148	3%
June 30, 2000	25,413	100,291	395%
June 30, 1999	24,241	8,918	37%
June 30, 1998	23,611	5,858	25%
June 30, 1997	13,179	5,917	45%

**PASADENA FIRE AND POLICE RETIREMENT SYSTEM
NOTES TO REQUIRED SUPPLEMENTAL INFORMATION
JUNE 30, 2006**

The information presented in the required supplemental schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows:

Valuation date	June 30, 2006
Actuarial cost method	Entry Age Normal
Amortization method	Level dollar
Remaining amortization period	5 years
Asset valuation method	5-year smoothed market
Actuarial assumptions:	
	Interest 8.0%
	Salary scale 5.6%
	Cost of living 4.0%

**PASADENA FIRE AND POLICE RETIREMENT SYSTEM
OTHER SUPPLEMENTAL INFORMATION
REVENUES BY SOURCE AND EXPENSES BY TYPE
(AMOUNTS IN THOUSANDS)**

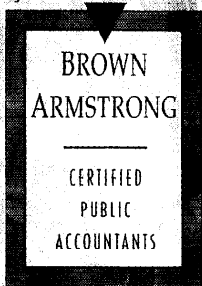
REVENUES BY SOURCE

<u>Fiscal Year</u>	<u>Employee Contributions</u>	<u>Employer Contributions</u>	<u>Investment Income (Loss)</u>	<u>Total</u>
2006	\$ 57	\$ 1,427	\$ 14,398	\$ 15,882
2005	82	26,293	13,635	40,010
2004	355	13,863	15,519	29,737
2003	371	212	2,772	3,355
2002	412	148	(8,945)	(8,385)
2001	664	148	(1,664)	(852)
2000	186	100,291	(14,543)	85,934
1999	455	8,918	5,815	15,188
1998	522	5,858	9,757	16,137
1997	529	5,917	9,707	16,153

Note: Employer contributions listed under actuarial valuation data for 2004 differ from employer contributions listed under financial statement data due to exclusion for actuarial valuation purposes of contributions receivable due under the Settlement Agreement and inclusion of a receivable from the June 2004 debenture (see Note 7).

EXPENSES BY TYPE

<u>Fiscal Year</u>	<u>Benefits</u>	<u>Administrative Expenses</u>	<u>Investment Expenses</u>	<u>Total</u>
2006	\$ 14,190	\$ 234	\$ 561	\$ 14,985
2005	13,969	229	457	14,655
2004	12,879	302	524	13,705
2003	12,751	225	542	13,518
2002	12,343	225	591	13,159
2001	12,019	254	532	12,805
2000	11,794	251	641	12,686
1999	11,714	235	375	12,324
1998	11,410	256	375	12,041
1997	11,170	104	337	11,611



BROWN ARMSTRONG
PAULDEN McCOWN STARBUCK THORNBURGH & KEETER
CERTIFIED PUBLIC ACCOUNTANTS

■ Main Office
4200 Truxtun Ave., Suite 300
Bakersfield, California 93309
Tel 661-324-4971 Fax 661-324-4997
e-mail: info@bacpas.com

■ Shafter Office
560 Central Avenue
Shafter, California 93263
Tel 661-746-2145 Fax 661-746-1218

Andrew J. Paulden, CPA
Peter C. Brown, CPA
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**AGREED UPON CONDITIONS REPORT DESIGNED TO INCREASE
EFFICIENCY, INTERNAL CONTROLS AND/OR FINANCIAL REPORTING**

To the Board of Retirement of the
Pasadena Fire and Police Retirement System

We have audited the financial statements of the Pasadena Fire and Police Retirement System (PFPRS) for the year ended June 30, 2006 and have issued our report thereon dated August 31, 2006. In planning and performing our audit of the financial statements of PFPRS, we considered its internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control structure.

As a result of our audit, we noted certain agreed-upon findings. These findings and recommendations, all of which have been discussed with the appropriate members of management, are intended to improve the internal control structure or result in other efficiencies and are summarized as follows:

Current Year Findings & Recommendations

Agreed Upon Condition 1 – Investment Manager Fees

During our analysis of professional fees, we noted that the fees for RREEF were not being properly booked to the expense account, but rather to the unrealized gain and loss account.

Recommendation

PFPRS should segregate the management fees for RREEF and book them to the appropriate expense account.

Management Response

Management concurs with the recommendation that the management fees should be expensed rather than netted against unrealized gains or losses.

Agreed Upon Condition 2 – Reconciliation of Investments

During our analysis of investments, we noted that investment managers with separately managed accounts are not required to reconcile market and cost of investments to the custodian.

Recommendation

Reconciliations between the information reported by Northern Trust and the information reported by the individual managers should be prepared on a monthly basis. The reconciling items should be fully explained. PFPRS staff should review these reconciliations for accuracy.

Management Response

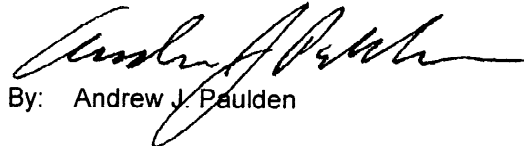
We have contacted both Met West Asset Management and Dodge & Cox who have the separately managed accounts for the FPRS. We have requested that they send us their monthly reconciliations to the Northern Trust Bank statements for their individual accounts. They informed us they reconcile to Northern Trust but we had not requested the copies of their reconciliations. We are now receiving them on a monthly basis and we are reviewing the reports for accuracy.

Status of Prior Year Findings & Recommendations

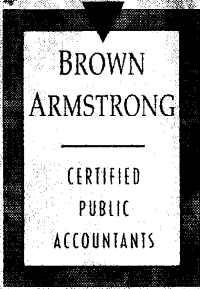
None.

This information is intended solely for the use of the Board of Retirement and management of PFPRS and should not be used for any other purpose. However, this report is a matter of public record, and its distribution is not limited.

BROWN ARMSTRONG PAULDEN
McCOWN STARBUCK THORNBURGH & KEETER
ACCOUNTANCY CORPORATION


By: Andrew J. Paulden

Bakersfield, California
August 31, 2006



BROWN ARMSTRONG
PAULDEN McCOWN STARBUCK THORNBURGH & KEETER
CERTIFIED PUBLIC ACCOUNTANTS

Main Office
4200 Truxtun Ave., Suite 300
Bakersfield, California 93309
Tel 661-324-4971 Fax 661-324-4997
e-mail: info@bacpas.com

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**REPORTABLE CONDITION LETTER
REGARDING INTERNAL CONTROL**

To the Board of Retirement of the
Pasadena Fire and Police Retirement System

In planning and performing our audit of the financial statements of the Pasadena Fire and Police Retirement System (PFPRS) for the year ended June 30, 2006, we considered its internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on internal control structure. We noted no matters involving internal control and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control that, in our judgment, could adversely affect the organization's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. We noted no reportable conditions which we considered to be material weaknesses.

Current Year Reportable Conditions

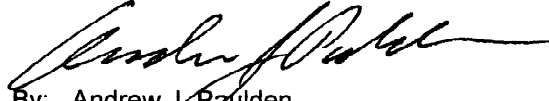
None.

Status of Prior Year Reportable Conditions

None.

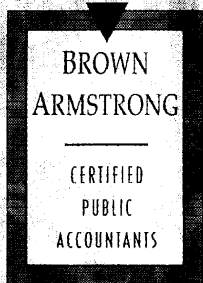
This information is intended solely for the use of the Board of Retirement and management of PFPRS and should not be used for any other purpose. However, this report is a matter of public record, and its distribution is not limited.

BROWN ARMSTRONG PAULDEN
McCOWN STARBUCK THORNBURGH & KEETER
ACCOUNTANCY CORPORATION



By: Andrew J. Paulden

Bakersfield, California
August 31, 2006



BROWN ARMSTRONG
PAULDEN McCOWN STARBUCK THORNBURGH & KEETER
CERTIFIED PUBLIC ACCOUNTANTS

Main Office
4200 Truxtun Ave., Suite 300
Bakersfield, California 93309
Tel 661-324-4971 Fax 661-324-4997
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**REQUIRED COMMUNICATION TO THE AUDIT COMMITTEE
IN ACCORDANCE WITH PROFESSIONAL STANDARDS**

To the Board of Retirement of the
Pasadena Fire and Police Retirement System

We have audited the financial statements of the Pasadena Fire and Police Retirement System (PFPRS) for the year ended June 30, 2006, and have issued our report thereon dated August 31, 2006. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility under U.S. Generally Accepted Auditing Standards

Our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement and are fairly presented in accordance with U.S. generally accepted accounting principles. Because an audit is designed to provide reasonable, but not absolute, assurance and because we did not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by us.

As part of our audit, we considered the internal controls of PFPRS. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal controls.

Significant Accounting Policies

Management has the responsibility for selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the PFPRS are described in the notes to the financial statements.

We noted no transactions entered into by PFPRS during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimate affecting the financial statements was the fair market value of investments.

Management's estimate of the fair market value of investments is derived by various methods as detailed in the notes to the financial statements. We evaluated the key factors and assumptions used to develop the fair market value of investments in determining that they are reasonable in relation to the financial statements taken as a whole.

Significant Audit Adjustments

For purposes of this letter, professional standards define an audit adjustment as a proposed correction of the financial statements that, in our judgment, may not have been detected except through our auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on PFPRS' financial reporting process (that is, cause future financial statements to be materially misstated). We did not propose audit adjustments that could in our judgment, either individually or in the aggregate, have a significant effect on PFPRS' financial reporting process.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to PFPRS' financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Issues Discussed Prior to Retention of Independent Auditors

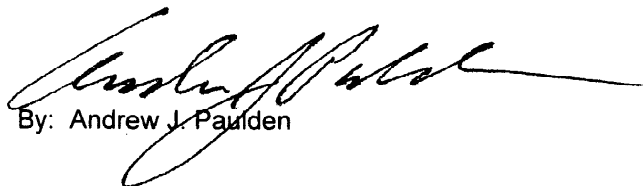
We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as PFPRS' auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Difficulties Encountered in Performing the Audit

We encountered no difficulties in dealing with management in performing our audit.

This information is intended solely for the information and use of the Board of Retirement, and management of PFPRS and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record, and its distribution is not limited.

BROWN ARMSTRONG PAULDEN
McCOWN STARBUCK THORNBURGH & KEETER
ACCOUNTANCY CORPORATION



By: Andrew J. Paulden

Bakersfield, California
August 31, 2006