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, 2010 AND 2009

PASADENA FIRE AND POLICE RETIREMENT SYSTEM
FOR THE YEARS ENDED JUNE 30, 2010 AND 2009
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INDEPENDENT AUDITOR'S REPORT

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

We have audited the accompanying statement of plan net assets of the Pasadena Fire and Police Retirement System (the "System") as of June 30, 2010 and 2009, and the related statement of changes in plan net assets for the years then ended. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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, 2010 and 2009, and the changes in plan net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis as listed in the table of contents be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

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 supplemental 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 7, 2010, on our consideration of the System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

Bakersfield, California
October 7, 2010

The Pasadena Fire and Police Retirement System ("System", or "Plan") is a defined benefit Plan governed by a Retirement Board ("Board") under the provisions of the City of Pasadena ("City") Charter. Its operations have been reported as a Pension Trust Fund in the City's financial statements. The System is a closed, single employer, defined benefit pension plan that continues to provide retirement, disability and survivor benefits for eligible sworn safety employees of the City. The System serves the City's sworn employees hired prior to July 1, 1977, except those who elected to transfer to the California Public Employees Retirement System ("CalPERS") either when the System was 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 System is governed by a Board of five trustees; one member of the City Council, two Pasadena residents appointed by the City Council, and two 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. Trustees receive no compensation.

The discussion and analysis of the System's financial performance provides an overview of the financial activities for the fiscal year ending June 30, 2010. 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 Management Discussion and Analysis. The financial statements, footnotes, and this discussion and analysis were prepared by management and are the responsibility of management.

Financial Highlights

The Change in Plan Net Assets Held in Trust for Pension Benefits increased by $4,707,307 for fiscal year 2010, which compares to a decrease of $37,755,231 in fiscal year 2009. This was driven by investment gains of $14,946,559 due to the recovery from the 2008 financial crisis in the economic and financial markets. The fiscal year saw a turnaround in the capital markets as the major equity indices across the globe experienced double-digit gains reversing the losses from 2008.

Due to the rebound in financial markets, net investment gains for the Plan were $14,946,559 as compared to the net investment loss of $23,625,543 in the prior fiscal year. The current fiscal year investment gains and losses from the prior year were consistent with overall market conditions.

Asset allocation is frequently reviewed by the Board and the investment consultant. An asset allocation study was conducted in 2008 and 2009 with the Board adopting a new asset allocation at their May 21, 2009, meeting, which was implemented in late June 2009. Overall, the allocations remained consistent with the prior policy target with the exception of creating a cash account and diversifying the relative risk within the domestic equity space by adding passive Large Cap Growth and Small-Mid Cap Core mandates. The decision to fund a cash reserve within the Plan was made to meet the required monthly cost of benefits and administration. The Board approved a plan to rebalance the portfolio quarterly to determine whether distributions are needed to pay the benefits and administrative costs. Prior to the completion and funding of the cash account, withdrawals from the fixed income and international funds were made monthly during the year to meet the required $1,350,000 payment of benefits and expenses. The monthly withdrawal was discontinued in June 2009, and the payments for June were paid out of the excess in the System's pooled cash account at the City. For fiscal year 2010, cash withdrawals were made from the Northern Trust Collective Government Short-Term Investment Fund (cash account) and transferred to the City's pooled cash account. Assets were liquidated from the accounts that exceeded their target allocation. This is an ongoing process to maintain balance with the Board's asset allocation goals and to fund the Plan's benefit and administrative costs.

Contributions for the fiscal year were $4,981,704, which consisted of a contribution that was received from the City under Contribution Agreement No. 16,900 ("Contribution Agreement").

Deductions from the Plan Net Assets primarily consisted of the payment of benefits to retired members and their beneficiaries and the costs of administering the Plan. These deductions increased to $15,220,956 in the current fiscal year. This represented an increase of $111,640 compared to the prior year and was primarily due to increased benefits and administrative costs.

The System engaged Bartel Associates on July 22, 2010, to serve as its independent actuary. The most recent actuarial valuation was prepared as of June 30, 2010, and determined the funded percentage, calculated in accordance with the Contribution Agreement, to be 66.1% as compared to 67.2% in the prior year. The decrease was attributable to the effect of recognizing a portion of the current year's investment losses which increased the overall funded position by 1.3%, the normal operation of the Plan including the continuing recognition of investment losses from prior years which decreased the funded percentage by 3.0%, and demographic losses which increased the funded percentage by 0.6%. The Plan had a market asset rate of return of 17.9% which exceeded the assumed rate of return of 8.0%.

As provided by the Contribution Agreement, if the funded percentage is below the minimum funding percentage of 75.0% for fiscal year 2010, the City will reimburse the System in the following fiscal year subject to certain reimbursement limits. Based on the June 30, 2010, actuarial valuation, the minimum funding deficit was $14,832,000, or 8.9%, below the funding requirement of 75.0% as of June 30, 2010. This compared to a minimum funding deficit of $12,908,520 to meet the minimum funding requirement of 74.5% as of June 30, 2009. 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 $8,036,000 and is due to the System no later than January 3, 2011.

Financial Statement Overview

This discussion and analysis serves as an introduction to the System's basic financial statements. These include the following three components:

- Statement of Plan Net Assets
- Statement of Changes in the Plan Net Assets
- Notes to Financial Statements

In addition to the financial statements, this report also contains required supplemental information and supporting schedules of actuarial information.

The *Statement of Plan Net Assets* provides a snapshot of account balances at year-end. It also indicates the assets available for future benefit payments and administration of the Plan as well as current liabilities outstanding at year-end. The assets less liabilities, give the reader a clear picture of what funds are available for future payments.

The *Statement of Changes in Plan Net Assets,* in contrast, provides a summary view of the additions to and the deductions from the plan net assets that occurred over the course of the year.

Together these two statements report the System's net assets–the difference between assets and liabilities–as one way to measure the System's financial position. Over time, increases and decreases in net assets are one indicator of whether the System's financial situation is improving or deteriorating. Additional factors, such as market conditions, also need to be considered in assessing the System's overall financial situation.

The financial statements and required disclosures are in compliance with the accounting principles and reporting guidelines as set forth by the Governmental Accounting Standards Board, using the accrual basis of accounting. Investments are reported at current fair value. Both realized and unrealized investment gains and losses are recognized.

The *Notes to Financial Statements* provide additional information and explanations that are essential to a full understanding of the data provided in the financial statements. The Notes to Financial Statements appear on pages 9 to 22.

The Required Supplemental Information follows the notes showing the Plan's funding progress with obligations to provide pension benefits to members, as well as historical trend information reflecting how much the City has contributed in relation to their annual required contributions.

Condensed Statement of Plan Net Assets

	June 30, 2010	June 30, 2009	June 30, 2008	Increase (Decrease) 2010/2009	Increase (Decrease) 2009/2008
	(In Thousands)				
Current Assets	$ 6,870	$ 11,932	$ 1,635	$ (5,062)	$ 10,297
Investments	85,113	75,324	123,417	9,789	(48,093)
Total Assets	91,983	87,256	125,052	4,727	(37,796)
Total Liabilities	67	47	47	20	-
Total Plan Net Assets	$ 91,916	$ 87,209	$ 125,005	$ 4,707	$ (37,796)

As of June 30, 2010, the System had $91,916,334 in Plan Net Assets. The Net Assets represent funds held in trust for future benefit 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

	June 30, 2010	June 30, 2009	June 30, 2008	Increase (Decrease) 2010/2009	Increase (Decrease) 2009/2008
	(In Thousands)				
Employer Contributions	$ 4,982	$ 956	$ 3,194	$ 4,026	$ (2,238)
Plan Member Contributions	-	24	24	(24)	-
Net Investment Income (Loss)	14,947	(23,626)	(10,399)	38,573	(13,227)
Total Additions (Decreases)	19,929	(22,646)	(7,181)	42,575	(15,465)
Benefit Payments	14,975	14,898	14,864	77	34
Administrative Expenses	246	211	301	35	(90)
Total Deductions	15,221	15,109	15,165	112	(56)
Net Increase (Decrease)	$ 4,708	$ (37,755)	$ (22,346)	$ 42,463	$ (15,409)

During the year ended June 30, 2010, the Plan Net Assets increased by $4,707,307, principally as a result of the increase in the System's investment performance, which coincided with the overall recovery in the U.S. and global financial markets, as well as the payments of the regularly scheduled benefits and System costs.

Fiduciary Responsibilities

The System is a fiduciary for the pension plan of the City of Pasadena. Accordingly, the System is responsible for ensuring that the assets reported in the statements are used for the intended purpose of paying expenses and providing retirement benefits to the retirees and beneficiaries of the System.

Requests for Information

This financial report is designed to provide a general overview of the System's finances and to account for the money the System receives. Questions concerning any of the information provided in this report or requests for additional information should be addressed to:

Pasadena Fire & Police Retirement System
100 N. Garfield Avenue, #N204
Pasadena, CA 91101

Respectfully submitted,

Mary Smith
Retirement Administrator

PASADENA FIRE AND POLICE RETIREMENT SYSTEM
STATEMENTS OF PLAN NET ASSETS
JUNE 30, 2010 AND 2009

	2010	2009
Assets		
Cash and cash equivalents	$ 6,687,696	$ 11,699,916
Receivables:		
Interest	183,072	231,542
Total receivables	183,072	231,542
Investments, at fair value:		
Government and agencies	14,252,981	11,043,617
Domestic corporate obligations	17,028,652	16,900,799
International corporate obligations	1,173,230	941,454
Real Estate (REITS)	6,134,669	4,035,853
Domestic corporate stocks	36,608,441	33,647,369
International corporate stocks	9,914,568	8,755,287
Total investments	85,112,541	75,324,379
Total assets	91,983,309	87,255,837
Liabilities		
Accounts payable and accrued liabilities	66,975	46,809
Total liabilities	66,975	46,809
Net assets held in trust for employees' pension benefits	$ 91,916,334	$ 87,209,028

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, 2010 AND 2009

	2010	2009
Additions:		
Contributions:		
Employer	$ 4,981,704	$ 956,097
Plan members	-	23,531
Total contributions	4,981,704	979,628
Net investment income (loss):		
Net changes in fair value of investments	12,986,543	(26,461,586)
Interest	1,517,524	2,052,803
Dividends	774,255	1,248,986
Gross investment income (loss)	15,278,322	(23,159,797)
Less investment expenses	(331,763)	(465,746)
Net investment income (loss)	14,946,559	(23,625,543)
Total additions (decreases)	19,928,263	(22,645,915)
Deductions:		
Benefits paid to participants	14,974,640	14,898,488
Administrative expenses	246,316	210,828
Total deductions	15,220,956	15,109,316
Net increase (decrease)	4,707,307	(37,755,231)
Net assets held in trust for employees' pension benefits:		
Beginning of year	87,209,027	124,964,259
End of year	$ 91,916,334	$ 87,209,028

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

NOTE 1 – PENSION PLAN DESCRIPTION

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 Retirement Board has sole and exclusive responsibility over the assets of the System and the responsibility to administer the System to assure prompt delivery of benefits and related services as provided in Article XV of the Pasadena City Charter. The Board consists of five members. The Board members as of June 30, 2010 were as follows:

Keith Jones, Chair
John Tennant, Vice Chair
Peter Boyle, Board Member
John Brinsley, Board Member
Steve Haderlein, Board Member

The System 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 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. The System provides basic lifetime retirement, disability and death benefits to members who meet the minimum age and length-of-service requirements.

As of June 30, 2010, the System membership consisted of 275 retirees and beneficiaries who currently receive benefits. There are no longer any active employees participating in the System. As of June 30, 2009, there were 290 retirees and beneficiaries.

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

Pension Plan Benefits

Members are entitled to annual pension benefits beginning at normal retirement age (50) equal to 1/50 of final compensation, times the member's number of years of service, times an actuarial equivalent based on the actual retirement age. The System 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.

Death Benefits

In the case of a death before a member is eligible to retire, there is a refund of the employee contributions, with interest, plus six months' salary. If the member is eligible to retire, 60% of the earned benefit is payable to the eligible surviving spouse for their lifetime.

NOTE 1 – PENSION PLAN DESCRIPTION (Continued)

Survivor Benefits

Upon the death of a retiree, the qualified beneficiary is entitled to receive retirement benefits equal to 60% continuance for a service retirement and 100% continuance for a service-connected disability retirement.

Cost of Living Adjustment (COLA)

Monthly retiree benefits are eligible for an annual cost of living adjustment based on the increase/decrease of the annual average in the Consumer Price Index (CPI) for the Los Angeles-Riverside-Orange County, CA area for the previous year, January to December, and the change is rounded to the nearest whole. The adjustments are calculated by the actuary, adopted by the Board and become effective on July 1 of each year. The COLA for 2010 was a decrease of 1% and 2009 was an increase of 4%.

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 and presented 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 System.

Estimates

The preparation of financial statements in accordance 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.

Reporting Entity

The System's annual audited financial statements are included in the City of Pasadena's financial reports as a pension trust fund.

Cash and Cash Equivalents

The System's cash and short-term investments are managed by the Northern Trust Bank (master custodian for investment securities) and the City Treasurer.

City Treasury

Cash necessary for the System's daily operations is pooled with other City funds for short-term investment by the City Treasurer. The City is responsible for the control and safekeeping of all instruments of title and for all investment of the pooled funds.

The System has designated $1,350,000 in cash reserves to be invested by the City Treasurer in pooled cash. The funds equal one month of benefits and administrative expenses and are restricted for use in the event of a major emergency or disaster.

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 2 – <u>SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES</u> (Continued)

<u>New Accounting Pronouncements</u>

The GASB issued Statement No. 51, "Accounting and Financial Reporting for Intangible Assets." This statement establishes accounting and financial reporting requirements for intangible assets, including easements, water rights, timber rights, patents, trademarks, and computer software. This statement was not required to be implemented by the System due to the lack of intangible assets on the Systems' books as of June 30, 2010.

The GASB issued Statement No. 53, "Accounting and Financial Reporting for Derivative Instruments." This statement establishes accounting and financial reporting requirements for derivative instruments entered into by state and local governments. This statement requires most derivative instruments to be measured at fair value and reported on the statement of net assets. GASB Statement No. 53 also establishes disclosure requirements, which include summary information of derivative instruments and the government's exposure to financial risks. This statement was not required to be implemented by the System due to the current investment policy not allowing the use of derivatives as of June 30, 2010.

NOTE 3 – <u>INVESTMENTS</u>

Investments are reported at fair market value. Fair value for investments of publicly traded stocks and bonds and issues of the U.S. Government and its agencies is based on the last reported sale price as of the fiscal year end. Fair value of securities denominated in a foreign currency reflects exchange rates in effect at fiscal year end. Fair value of investments in commingled funds in real estate is based on the fund share price provided by the fund manager which is based on net asset value.

<u>Authorized Investments</u>

The City of Pasadena Charter confers the authority and fiduciary responsibility for investing the System's funds on the Retirement Board. In addition, as set forth below, Board members are subject to carry out their duties in the manner of a prudent person familiar with such retirement and investment matters acting under similar circumstances. 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. This prudent expert rule permits the Board to make investment allocation decisions and diversify investment holdings to reduce overall risk and increase returns. The prudent expert rule also permits the Board to establish an investment policy based on professional advice and counsel, and allows for the delegation of investment authority to professional investment managers. The System's investment policy outlines the responsibility for the investment of the funds and the degree of risk deemed appropriate for the System's investments. Investment managers are contractually bound to carry out their responsibilities in accordance with the Board of Retirement's investment policy and to follow specific contractual guidelines.

The Board oversees and guides the System 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.
- Diversify the investments of the System 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.

NOTE 3 – INVESTMENTS (Continued)

Authorized Investments (Continued)

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
- Corporate and Municipal Bonds
- Preferred stock
- Common stock
- Fixed-income funds
- Foreign stock and corporate bonds
- Mutual funds
- Real Estate Investment Trust (REIT)

Deposit and Investment Risks

The System adopted GASB Statement No. 40, Deposit and Investment Risk Disclosures – an amendment to GASB Statement No. 3, effective July 1, 2004. GASB 40 is designed to inform financial statement users about deposit and investment risks that could affect the ability to provide services and meet obligations as they become due. The disclosures required by this Statement provide information to assess common risks inherent in deposit and investment transactions. Deposit and investment resources represent considerable assets of the System, and these resources are necessary to carry out fiduciary responsibilities. GASB 40 requires the disclosure of the following specific risks that apply to the System's investments:

Credit Risk and Market Value of Investments
Custodial Credit Risk – Deposits and Investments
Concentration of Credit Risk
Interest Rate Risk
Highly Sensitive Investments
Foreign Currency Risk
Cash and Investments

GASB Statement No. 40 also requires the disclosure of deposit or investment policies (or the lack thereof) that relate to the investment and custodial risks that are required to be disclosed.

NOTE 3 – INVESTMENTS (Continued)

Statement of Investment Policy

The Board has chosen to manage the investment risks described by GASB No. 40 by contractually requiring each portfolio investment manager to abide by the Statement of Investment Policy, specifically tailored to that individual manager, rather than adopting across-the-board investment policies with respect to these investment risks. The Board adopted its revised Statement of Investment Policy on May 21, 2009, with a revision on September 17, 2009. A revision was adopted on May 20, 2010, which extended the strategic allocation ranges for equities. At the end of June 30, 2010, the System had six external investment managers.

The fixed income policy stipulates the strategy and investments, investment process, quality constraints, duration constraints, diversification, cash reserves, derivatives, and rate of return expectation.

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 Statement of Investment Policy, effective May 21, 2009, with revisions on September 17, 2009, and May 20, 2010, in accordance with applicable local, State, and Federal laws. The Board members exercise authority and control over the management of the System's assets by setting policy which the Board executes through the use of external prudent experts. The Board oversees and guides the System 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.
- Diversify the investments of the System 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 Statement of Investment Policy encompasses the following asset classes and the asset allocation goals:

- Domestic Core Fixed Income – 35%
- Large Cap Domestic Equity – 30% (15% Large Cap Value, 15% Large Cap Growth - Passive)
- Small-Mid Cap Core Equity – 10%
- International Equity – 12%
- Real Estate Investment Trust (REIT) – 8%
- Cash – STIF – 5%

The System requires $1,350,000 monthly to cover the benefit payments and administrative costs. When an asset class exceeds the allocation goal, the Board and Investment Consultant review the allocation and determine the appropriate asset class/classes from which to withdraw the cash. This also serves as an ongoing rebalancing of the fund to maintain the allocation goals.

NOTE 3 – INVESTMENTS (Continued)

Credit Risk

Credit Risk is the risk that the issuer of a debt security or other counterparty to an investment will not fulfill its obligations. The individual investment guidelines for the fixed income investment manager describe applicable restrictions on credit risk. 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, 2010, are as follows:

Credit Quality Ratings of Investments in Fixed Income Securities

Quality Ratings - S & P	Market Value	Percentage
AAA	$ 7,413,164	22.84%
AA	1,366,443	4.21%
A	5,405,673	16.66%
BBB	3,144,866	9.69%
BB	863,292	2.66%
B	892,491	2.75%
CCC	816,482	2.52%
CC	106,060	0.33%
Not Rated/Quality Rating NA*	816,111	2.51%
Rating Not Determined **	11,630,281	35.84%
Total	$ 32,454,863	100.00%

* Minus: Not rated: STIF of $6,382,119 and commercial paper of $434,979.

** Minus: Not rated: Short Term Bills/Notes of $744,507.

** These ratings are implicitly or explicitly guaranteed by the US Government and currently a rating is not provided by the nationally recognized statistical rating organization. The rating agencies normally do not rate government agency and treasury debt and therefore they have an implied AAA rating.

Custodial Credit Risk – Deposits

Custodial credit risk for deposits is the risk that, in the event of a financial institution's failure, the System will not be able to recover the value of deposits nor 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, 2010, the System is not exposed to such risk on the fair value of total international investments. The System does not have a formal policy for custodial credit risk.

Custodial Credit Risk – Investments

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the System will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. The individual investment guidelines for each investment manager require that managed investments be held and maintained with the master custodian in the name of the System. Investment securities are exposed to custodial credit risk if the securities are uninsured, 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 because all securities are held by the System's custodial bank in the System's name.

NOTE 3 – INVESTMENTS (Continued)

Concentration of Credit Risk

Concentration of Credit Risk is the risk of potential loss attributed to the magnitude of the System's investment in a single issuer of securities. The individual investment guidelines for the fixed income manager forbid concentrations greater than 5% in the securities of any one issuer (excepting issues issued by or explicitly guaranteed by the U.S. government). As of June 30, 2010, the System's portfolio did not hold any investments in any one issuer that would represent five percent (5%) or more of the System's net assets.

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 uses the present values of cash flows, weighted for those cash flows as a percentage of the investment's full price. The longer the duration of a portfolio, the greater its price sensitivity is to changes in interest rates.

While no specific ranges are required, one of the ways the System manages its exposure to interest rate risk is by requiring the fixed income investment manager to maintain their portfolio effective duration within +/- 20% of the benchmark, the Barclays Capital US Aggregate Bond Index. 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, 2010

Investment Type	**Market Value**	**Duration**
U.S. Government and Agency Instruments		
Government Bonds	$ 6,090,920	5.50
Government Mortgage Backed Securities	7,848,687	3.83
Government Issued Commercial Mortgage Backed Securities	139,206	8.77
Municipal/Provincial Bonds	174,168	11.38
Total	14,252,981	
Corporate Securities		
Corporate Bonds	7,617,367	4.64
Non-Government Backed C.M.O.'s	3,779,826	1.83
Asset Backed Securities	2,720,058	1.92
Commercial Mortgage Backed Securities	2,395,239	5.53
Index Linked Government Bonds	1,363,314	7.02
Guaranteed Fixed Income	272,398	0.09
Other Fixed Income (Eff. Duration unavailable)	53,680	N/A
Total	18,201,882	
Total Fixed Income Securities	$ 32,454,863	

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:

Investment Type	Amount
Government Mortgage Backed Securities	$ 7,848,687
Government Issued Commercial Mortgage Backed Securities	139,206
Asset Backed Securities	2,720,058
Commercial Mortgage Backed Securities	2,395,239
Non-Government Backed Commercial Mortgage Obligations	3,779,826
Total	$ 16,883,016

Foreign Currency Risk

Foreign currency risk is the risk that changes in foreign exchange rates will adversely affect the fair value of an investment or deposit. The System's authorized investment managers are permitted to invest in approved countries or regions, as stated in their respective investment guidelines. Currency hedging will be permitted as part of a defensive strategy to protect the portfolio's underlying assets.

The System's investment holdings as of June 30, 2010, are as follows:

Foreign Currency Type - Corporate Bonds	Market Value in USD	% of Total MV
Australia	$ 140,509	0.16
Bermuda	82,599	0.09
Germany	224,224	0.25
Guernsey, Channel Islands	120,836	0.13
United Kingdom	271,175	0.30
Switzerland	156,625	0.17
New Zealand	177,262	0.20
Total Foreign Currency	$ 1,173,230	1.30
Foreign Currency Type - Equities		
International Region	$ 9,914,568	10.98
Total Foreign Currency	$ 9,914,568	10.98

NOTE 3 – INVESTMENTS (Continued)

Cash and Investments

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

	June 30, 2010	June 30, 2009
	(In Thousands)	
Unrestricted Pooled Cash	$ 370	$ 1,608
Restricted Pooled Cash	1,350	1,350
Cash with Fiscal Agent	4,967	8,742
Investments - Held by Trustee	85,112	73,324
	$ 91,799	$ 85,024

NOTE 4 – CONTRIBUTION INFORMATION

Contribution requirements are established by the City Charter and by contract, and, subject to any constitutional limitations, may be amended by the City Charter or further agreement between the City and the System.

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 No. 16,900, dated March 18, 1999, between the City and the 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.

NOTE 4 – CONTRIBUTION INFORMATION (Continued)

Member Contributions

As a condition of participation, members were required to contribute the following percentage of their annual salary to the System. Currently there are no active members in the System, and hence no further member contributions are due to the System.

Age of Entry Into the System	Percent of Annual Salary Contributed
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 System 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 exceeded 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 for the active members regardless of the funding status of the System. 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.

Active members were also required to make cost-of-living contributions, as a percent of covered salary, which amounted to 5% for 2010 and 2009, and is matched 100% by the City. These contributions by active members were to be made as long as the funding percentage was 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. Because there were no active members, accumulated contributions at June 30, 2010 and 2009, were $0 and $0, respectively, with no interest credited for 2010 and 2009.

NOTE 5 – ADMINISTRATIVE COSTS

The administrative costs to administer the System are paid by the System. Administrative expenses were $246,316 and $210,829, respectively, for 2010 and 2009.

NOTE 6 – SUPPLEMENTAL FUNDING PLAN

The System engages an independent actuary to perform an annual actuarial valuation. The results of the valuation as of June 30, 2010, are presented in the Schedule of Funding Progress. This includes historical trend information about the actuarially determined funded status of the System from a long-term ongoing System perspective; the progress made in accumulating sufficient assets to pay benefits when due; and the Schedule of Employer Contributions.

The latest annual valuation was performed as of June 30, 2010. 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 the 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 were different from such assumptions, an unfunded actuarial accrued liability had developed.

To fund the unfunded actuarial accrued 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, and agreed to make supplemental contributions to the System when needed.

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, 2000. The minimum funding percentage is increased by one-half of one percent for each of the 20 years after that.

As of June 30, 2010 and 2009, the funded percentage of the System, calculated in accordance with Contribution Agreement No. 16,900, was 66.1% and 67.2% respectively. The funded percentage for 2010 and 2009 was below the required minimum funding percentages of 75% and 74.5%, respectively. The Contribution Agreement states that if the System falls below the minimum funding percentage, the City will make supplemental contributions to 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.

NOTE 6 – <u>SUPPLEMENTAL FUNDING PLAN</u> (Continued)

The minimum funding deficits were $14,832,000 and $12,908,520 as of June 30, 2010 and 2009, 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, but no annual supplemental payment may exceed a reimbursement cap measured by the prior year's payments for benefits other than the funded basic benefits. The required supplemental contributions by the City as of June 30, 2010 and 2009 were $8,036,000 and $4,981,704, respectively. As provided by the Contribution Agreement, the contribution is due to the System in January of the subsequent fiscal year.

The information displayed below presents the funded status as of the most recent actuarial valuation. The Schedule of Funding Progress – Pension Plan in the Required Supplementary Information section immediately following the notes to the financial statements presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability of benefits.

Funded Status as of the Most Recent Actuarial Valuation Date
(Dollars in thousands)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll [(b-a)/c]
June 30, 2010	$ 109,740	$ 166,096	$ 56,356	66.1%	$ -	N/A

Actuarial Methods and Significant Assumptions

Valuation date	June 30, 2010	
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	No active employees
	Cost of living	3.8% (except for 1919 and 1935 benefits)

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, which the actuarial value of assets was required to stay within, to ensure that the actuarial value of the assets did 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. The City contributed this amount 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 of 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, subject to certain exceptions if actuarial standards or practices were changed, or the City failed to make any required contribution. As of June 30, 2005, $40,000,000 was collected by the System.

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 No. 16,900. The payments under the Settlement Agreement in excess of the amount allocated to the debenture and included in the System assets in the prior year were included in System 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 between the City and CalPERS. Ten members elected to transfer to CalPERS, and in July 2004 assets of $4,687,000 attributable to these members was transferred to CalPERS. These were recognized as payables in fiscal year 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 System are presented, where available, on the following pages as Required Supplementary Information.

NOTE 11 – SUBSEQUENT EVENTS

Subsequent to June 30, 2010, and through October 7, 2010, the date through which management evaluated subsequent events and on which the financial statements were issued, the System did not identify any subsequent events that require disclosure.

REQUIRED SUPPLEMENTAL INFORMATION

PASADENA FIRE AND POLICE RETIREMENT SYSTEM
SCHEDULE OF FUNDING PROGRESS
(AMOUNTS IN THOUSANDS)
JUNE 30, 2010

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	[(b-a)/c] UAAL as a % of Covered Payroll
June 30, 2010	$ 109,740	$ 166,096	$ 56,356	66%	$ -	N/A
June 30, 2009	119,551	177,803	58,252	67%	-	N/A
June 30, 2008	131,321	178,748	47,427	73%	179	26,506 %
June 30, 2007	131,137	183,046	51,909	72%	146	35,607 %
June 30, 2006	127,841	184,852	57,011	69%	141	40,416 %
June 30, 2005	132,730	185,181	52,451	72%	277	18,902 %

* 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).

PASADENA FIRE AND POLICE RETIREMENT SYSTEM
SCHEDULE OF EMPLOYER CONTRIBUTIONS
(AMOUNTS IN THOUSANDS)
JUNE 30, 2010

Fiscal Year Ended	Annual Required Contribution	Actual Contribution	Percentage of ARC Recognized as Contribution
June 30, 2010	$ 4,981	$ 4,981	100%
June 30, 2009	11,447	956	8%
June 30, 2008	12,525	3,194	25%
June 30, 2007	13,755	3,839	28%
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%

PASADENA FIRE AND POLICE RETIREMENT SYSTEM
NOTES TO REQUIRED SUPPLEMENTAL INFORMATION
JUNE 30, 2010

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, 2010	
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	No active employees
	Cost of living	3.8% (except for 1919 and 1935 benefits)

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

REVENUES BY SOURCE

Fiscal Year	Employee Contributions	Employer Contributions	Gross Investment Income (Loss)	Total
2010	$ -	$ 4,982	$ 15,278	$ 20,260
2009	24	956	(23,160)	(22,180)
2008	24	3,194	(9,992)	(6,774)
2007	20	3,839	22,343	26,202
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)

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

Fiscal Year	Benefits	Administrative Expenses	Investment Expenses	Total
2010	$ 14,975	$ 246	$ 332	$ 15,553
2009	14,898	211	466	15,575
2008	14,864	301	407	15,572
2007	14,572	257	492	15,321
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