VIRGINIA RETIREMENT SYSTEM
STATE EMPLOYEE RETIREMENT PLAN

GASB No. 68 Schedules

With Independent Auditor's Report Thereon

For the Fiscal Year Ended June 30, 2013

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Commonwealth of Virginia

Auditor of Public Accounts

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Auditor of Public Accounts

P.O. Box 1295
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October 1, 2015

The Board of Trustees
Fort Monroe Authority

Mr. Glen Oder, Executive Director, Fort Monroe Authority

The Board of Directors
Virginia Commonwealth University Health
System Authority

Independent Auditor's Report

Report on the Schedules

We have audited the accompanying schedule of employer allocations of the Virginia Retirement System State Employee Retirement Plan, as of and for the year ended June 30, 2013, and the related notes. Fort Monroe Authority (the Authority) and the Virginia Commonwealth University Health System Authority (the University Authority) are participating employers of the Virginia Retirement System State Employee Retirement Plan. We have also audited the total for all state employers of the column titled net pension liability included in the accompanying schedule of net pension liability of the Virginia Retirement System State Employee Retirement Plan as of and for the year ended June 30, 2013, and the related notes.

Management's Responsibility for the Schedule

The Virginia Retirement System's management is responsible for the preparation and fair presentation of these schedules in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the schedules that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on the schedule of employer allocations and the specified column total included in the schedule of net pension liability 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 schedule of employer allocations and the specified column total included in the schedule of net pension liability are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the schedule of employer allocations and the specified column total included in the schedule of net pension liability. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the schedule of employer allocations and the specified column total included in the schedule of net pension liability, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the schedule of employer allocations and the specified column total included in the schedule of net pension liability in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by the Virginia Retirement System management, as well as evaluating the overall presentation of the schedule of employer allocations and the specified column total included in the schedule of net pension liability.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

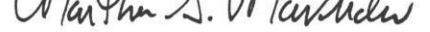
Opinions

In our opinion, the schedules referred to above present fairly, in all material respects, the employer allocations and the net pension liability, for the total of all participating state employers of the Virginia Retirement System State Employee Retirement Plan, for the year ended June 30, 2013, in accordance with accounting principles generally accepted in the United States of America.

Other Matter

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States, the financial statements of the Virginia Retirement System as of and for the year ended June 30, 2013, and our report thereon, dated December 2, 2013, expressed an unmodified opinion on those financial statements.

Our report is intended solely for the information and use of the Virginia Retirement System management, the Virginia Retirement System Board of Trustees, the Commonwealth Joint Legislative Audit and Review Commission, and the Authority's and University Authority's management and their auditors and is not intended to be and should not be used by anyone other than these specified parties.



AUDITOR OF PUBLIC ACCOUNTS

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Virginia Retirement System
VRS State Employee Retirement Plan
Schedule of Employer Allocations
For the Fiscal Year Ended June 30, 2013

Employer Code	Employer		Employer Contributions	Employer Allocation Percentage
30206	MCV HOSPITALS AUTHORITY	$	3,379,464	1.03839%
35885	FORT MONROE AUTHORITY		102,526	0.03150%
	ALL OTHER STATE AGENCIES		321,969,826	98.93011%
	Total for all State Employers	$	325,451,816	100.00000%

The accompanying notes are an integral part of the Schedule of Employer Allocations.

Virginia Retirement System
VRS State Employee Retirement Plan
Schedule of Net Pension Liability
As of June 30, 2013

(Dollars in Thousands)

Employer Code	Employer		Net Pension Liability June 30, 2013
30206	MCV HOSPITALS AUTHORITY	$	68,184
35885	FORT MONROE AUTHORITY		2,068
	ALL OTHER STATE AGENCIES		6,496,037
	Total for all State Employers	$	6,566,289

The accompanying notes are an integral part of the Schedule of Net Pension Liability.

Virginia Retirement System
VRS State Employee Retirement Plan
Notes to GASB No. 68 Schedules
For the Fiscal Year Ended June 30, 2013

Note 1. Summary of Significant Accounting Policies

Description of the Entity

The Virginia Retirement System (the System) is an independent agency of the Commonwealth of Virginia. The System administers four separate pension trust funds – the Virginia Retirement System (VRS), the State Police Officers' Retirement System (SPORS), the Virginia Law Officers' Retirement System (VaLORS), and the Judicial Retirement System (JRS). The VRS State Employee Retirement Plan is part of the VRS Trust Fund.

Administration and Management

The Board of Trustees (the Board) is responsible for the general administration and operation of the defined benefit pension plans and the other employee benefit plans. The Board has full power to invest and reinvest the trust funds of the System through the adoption of investment policies and guidelines that fulfil the Board's investment objective to maximize long-term investment returns while targeting and acceptable level of risk.

The Board consists nine members. Five members are appointed by the Governor and four members are appointed by the Joint Rules Committee of the General Assembly subject to confirmation by the General Assembly. The Board appoints a director to serve as the chief administrative officer of the System and a chief investment officer to direct, manage, and administer the investment of the System's funds.

The System issues a Comprehensive Annual Financial Report (CAFR) containing the financial statements and required supplementary information for all of the System's pension and other employee benefit trust funds. The CAFR is publically available through the About VRS link on the VRS website at www.varetire.org, or a copy may be obtained by submitting a request to the VRS Chief Financial Officer, PO Box 2500, Richmond, VA 23218-2500. The pension and other employee benefit trust funds administered by the VRS are classified as fiduciary funds and are included in the basic financial statements of the Commonwealth of Virginia.

Pensions

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Virginia Retirement System (VRS) State Employee Plan and the additions to/deductions from the VRS State Employee Retirement Plan's net fiduciary position have been determined on the same basis as they were reported by VRS. For this purpose, benefit payments (including refunds of employee contributions) are

recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Note 2. General Information about the Pension Plan

Plan Description

All full-time, salaried permanent employees of state agencies are automatically covered by VRS State Employee Retirement Plan upon employment. This plan is administered by the Virginia Retirement System (the System) along with plans for other employer groups in the Commonwealth of Virginia. The State Employee Retirement Plan is a single employer plan treated as a cost-sharing employer plan for financial reporting purposes. Members earn one month of service credit for each month they are employed and for which they and their employer are pay contributions to VRS. Members are eligible to purchase prior service, based on specific criteria a defined in the *Code of Virginia*, as amended. Eligible prior service that may be purchased includes prior public service, active military service, certain periods of leave, and previously refunded service.

During the fiscal year, the System administered two different benefit structures for covered employees in the VRS State Employee Retirement Plan – Plan 1 and Plan 2. Each of these benefit structures has a different eligibility criteria. The specific information for each plan, and the eligibility for covered groups within each plan are set out in the table below:

RETIREMENT PLAN PROVISIONS BY PLAN STRUCTURE	
PLAN 1	**PLAN 2**
About Plan 1 Plan 1 is a defined benefit plan. The retirement benefit is based on a member's age, creditable service and average final compensation at retirement using a formula. Employees are eligible for Plan 1 if their membership date is before July 1, 2010, and they were vested as of January 1, 2013.	**About Plan 2** Plan 2 is a defined benefit plan. The retirement benefit is based on a member's age, creditable service and average final compensation at retirement using a formula. Employees are eligible for Plan 2 if their membership date is on or after July 1, 2010, or their membership date is before July 1, 2010, and they were not vested as of January 1, 2013.
Eligible Members Employees are in Plan 1 if their membership date is before July 1, 2010, and they were vested as of January 1, 2013.	**Eligible Members** Employees are in Plan 2 if their membership date is on or after July 1, 2010, or their membership date is before July 1, 2010, and they were not vested as of January 1, 2013.

Retirement Contributions Employees contribute 5% of their compensation each month to their member contribution account through a pre-tax salary reduction. Member contributions are tax-deferred until they are withdrawn as part of a retirement benefit or as a refund. The employer makes a separate actuarially determined contribution to VRS for all covered employees. VRS invests both member and employer contributions to provide funding for the future benefit payment.	**Retirement Contributions** Employees contribute 5% of their compensation each month to their member contribution account through a pre-tax salary reduction.
Creditable Service Creditable service includes active service. Members earn creditable service for each month they are employed in a covered position. It also may include credit for prior service the member has purchased or additional creditable service the member was granted. A member's total creditable service is one of the factors used to determine their eligibility for retirement and to calculate their retirement benefit. It also may count toward eligibility for the health insurance credit in retirement, if the employer offers the health insurance credit.	**Creditable Service** Same as Plan 1.
Vesting Vesting is the minimum length of service a member needs to qualify for a future retirement benefit. Members become vested when they have at least five years (60 months) of creditable service. Vesting means members are eligible to qualify for retirement if they meet the age and service requirements for their plan. Members also must be vested to receive a full refund of their member contribution account balance if they leave employment and request a refund. Members are always 100% vested in the contributions that they make.	**Vesting** Same as Plan 1.

Calculating the Benefit The Basic Benefit is calculated based on a formula using the member's average final compensation, a retirement multiplier and total service credit at retirement. It is one of the benefit payout options available to a member at retirement. An early retirement reduction factor is applied to the Basic Benefit if the member retires with a reduced retirement benefit or selects a benefit payout option other than the Basic Benefit.	**Calculating the Benefit** See definition under Plan 1.
Average Final Compensation A member's average final compensation is the average of the 36 consecutive months of highest compensation as a covered employee.	**Average Final Compensation** A member's average final compensation is the average of their 60 consecutive months of highest compensation as a covered employee.
Service Retirement Multiplier The retirement multiplier is a factor used in the formula to determine a final retirement benefit. The retirement multiplier for members is 1.70%.	**Service Retirement Multiplier** Same as Plan 1 for service earned, purchased or granted prior to January 1, 2013. The retirement multiplier is 1.65% for creditable service earned, purchased or granted on or after January 1, 2013.
Normal Retirement Age Age 65.	**Normal Retirement Age** Normal Social Security retirement age.
Earliest Unreduced Retirement Eligibility Age 65 with at least five years (60 months) of creditable service or at age 50 with at least 30 years of creditable service.	**Earliest Unreduced Retirement Eligibility** Normal Social Security retirement age with at least five years (60 months) of creditable service or when their age and service equal 90.
Earliest Reduced Retirement Eligibility **VRS:** Age 55 with at least five years (60 months) of creditable service or age 50 with at least 10 years of creditable service.	**Earliest Reduced Retirement Eligibility** **VRS:** Age 60 with at least five years (60 months) of creditable service.

Cost-of-Living Adjustment (COLA) in Retirement The Cost-of-Living Adjustment (COLA) matches the first 3% increase in the Consumer Price Index for all Urban Consumers (CPI-U) and half of any additional increase (up to 4%) up to a maximum COLA of 5%. **<u>Eligibility:</u>** For members who retire with an unreduced benefit or with a reduced benefit with at least 20 years of creditable service, the COLA will go into effect on July 1 after one full calendar year from the retirement date. For members who retire with a reduced benefit and who have less than 20 years of creditable service, the COLA will go into effect on July 1 after one calendar year following the unreduced retirement eligibility date. **<u>Exceptions to COLA Effective Dates:</u>** The COLA is effective July 1 following one full calendar year (January 1 to December 31) under any of the following circumstances: • The member is within five years of qualifying for an unreduced retirement benefit as of January 1, 2013. • The member retires on disability. • The member Is involuntarily separated from employment for causes other than job performance or misconduct and is eligible to retire under the Workforce Transition Act or the Transitional Benefits Program. • The member dies in service and the member's survivor or beneficiary is eligible for a monthly death-in-service benefit. The COLA will go into effect on July 1 following one full calendar year (January 1 to December 31) from the date the monthly benefit begins.	**Cost-of-Living Adjustment (COLA) in Retirement** The Cost-of-Living Adjustment (COLA) matches the first 2% increase in the CPI-U and half of any additional increase (up to 2%), for a maximum COLA of 3%. **<u>Eligibility:</u>** Same as Plan 1 **<u>Exceptions to COLA Effective Dates:</u>** Same as Plan 1
Disability Coverage N/A	**Disability Coverage** N/A

Purchase of Prior Service Members may be eligible to purchase service from previous public employment, active duty military service, an eligible period of leave or VRS refunded service as creditable service in their plan. Prior creditable service counts toward vesting, eligibility for retirement and the health insurance credit. Only active members are eligible to purchase prior service. When buying service, members must purchase their most recent period of service first. Members also may be eligible to purchase periods of leave without pay.	**Purchase of Prior Service** Same as Plan 1.

Actuarial Assumptions and Methods

The total pension liability for the VRS State Employee Retirement Plan was based on an actuarial valuation as of June 30, 2013, using the Entry Age Normal actuarial cost method and the following assumptions:

Inflation	2.5 percent
Salary increases, including Inflation	3.5 percent – 5.35 percent
Investment rate of return	7.0 Percent, net of pension plan investment expense, including inflation*

* Administrative expenses as a percent of the market value of assets for the last experience study were found to be approximately 0.06% of the market assets for all of the VRS plans. This would provide an assumed investment return rate for GASB purposes of slightly more than the assumed 7.0%. However, since the difference was minimal, and a more conservative 7.0% investment return assumption provided a projected plan net position that exceeded the projected benefit payments, the long-term expected rate of return on investments was assumed to be 7.0% to simplify preparation of pension liabilities.

Mortality rates:

Pre-Retirement:

RP-2000 Employee Mortality Table Projected with Scale AA to 2020 with males set forward 2 years and females were set back 3 years.

Post-Retirement:

RP-2000 Combined Mortality Table Projected with Scale AA to 2020 with females set back 1 year.

Post-Disablement:

RP-2000 Disability Life Mortality Table Projected to 2020 with males set back 3 years and no provision for future mortality improvement

The actuarial assumptions used in the June 30, 2013 valuation were based on the results of an actuarial experience study for the four-year period from July 1, 2008 through June 30, 2012. Changes to the actuarial assumptions as a result of the experience study are as follows:

- Update mortality table
- Decrease in rates of service retirement
- Decrease in rates of withdrawals for less than 10 years of service
- Decrease in rates of disability for males
- Reduce rates of salary increase by 0.25% per year

Note 3. Net Pension Liability

The net pension liability (NPL) is calculated separately for each system and represents that particular system's total pension liability determined in accordance with GASB Statement No. 67, less that system's fiduciary net position. As of June 30, 2013, NPL amounts for the VRS State Employee Retirement Plan are as follows (amounts expressed in thousands):

Total Pension Liability	$ 21,068,651
Plan Fiduciary Net Position	14,502,362
Employers' Net Pension Liability (Asset)	$ 6,566,289
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	68.83%

The total pension liability is calculated by the System's actuary, and each plan's fiduciary net position is reported in the System's financial statements. The net pension liability is disclosed in accordance with the requirements of GASB Statement No. 67 in the System's notes to the financial statements and required supplementary information.

Discount Rate

The discount rate used to measure the total pension liability was 7.00%. The projection of cash flows used to determine the discount rate assumed that member contributions will be made per the VRS Statutes and the employer contributions will be made in accordance with the VRS funding policy at rates equal to the difference between actuarially determined contribution rates adopted by the VRS Board of Trustees and the member rate. Through the fiscal year ending June 30, 2018, the rate contributed by the state agencies for the VRS State Employee Retirement Plan will be subject to the portion of the VRS Board-certified rates that are funded by the Virginia General Assembly. From July 1, 2018 on, state agencies are assumed to contribute 100% of the actuarially determined contribution rates. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore the long-term expected

rate of return was applied to all periods of projected benefit payments to determine the total pension liability.

Note 4. Employer Contributions

Employers' proportionate shares were calculated on the basis of historical employer contributions. Although GASB Statement No. 68 encourages the use of the employer's projected long-term contribution effort to the retirement plan, allocating on the basis of historical employer contributions is considered acceptable. Employer contributions recognized by the VRS State Employee Retirement Plan that are not representative of future contribution effort are excluded in the determination of employers' proportionate shares. Examples of employer contributions not representative of future contribution effort are contributions toward the purchase of employee service, contributions for adjustments for prior periods, and supplemental employer contributions from certain employers.

The following table provides a reconciliation of the employer contributions in the VRS State Employee Retirement Plan's Statement of Changes in Fiduciary Net Position (per the System's separately issued financial statements) to the employer contributions used in the determination of employers' proportionate shares of collective pension amounts reported in the Schedule of Employer Allocations.

Employer Contributions Reported in the VRS State Employee Retirement Plan's Statement of Changes In Net Position for the fiscal year ended June 30, 2013	$ 326,226,000
Deduct: Employer Contributions Not Representative Of Future Contribution Effort	(774,814)
Employer Contributions Used as the Basis for Allocating Employers' Proportionate Shares of Collective Pension Amounts – June 30, 2013	$ 325,451,186

Note 5. Additional Financial and Actuarial Information

Information contained in the VRS State Employee Retirement Plan Notes to the Schedule of Employer Allocations and Schedule of Pension Amounts by Employer (Schedules) was extracted from the audited financial statement of the Virginia Retirement System for the fiscal year ended June 30, 2013. Additional financial information supporting the preparation of the VRS State Employee Retirement Plan Schedules (including the unmodified audit opinion on the financial statements and required supplementary information) is presented in the separately issued VRS 2013 Comprehensive Annual Financial Report (CAFR). A copy of the 2013 VRS CAFR is publicly available through the About VRS link on the VRS website at www.varetire.org, or a copy may be obtained by submitting a request to the VRS Chief Financial Officer, PO Box 2500, Richmond, VA 23218-2500.