
Joint Legislative Audit and Review Commission



**VRS Oversight: Biennial Status
and Semi-Annual Investment Report
December 2006**

Commission Briefing

December 11, 2006



JLARC

VRS Oversight Act

- Oversee and evaluate VRS on a continuing basis
- Prepare semi-annual investment reports
- Prepare a biennial status report
- Conduct a quadrennial actuarial analysis
- Publish an informational guide for legislators
- Hire an actuary for use by JLARC, House Appropriations, and Senate Finance

Fund Performance

- Total market value of fund assets on September 30, 2006, was **\$50.3 billion**
- VRS' investment returns have shown strong performance

One-Year Return	Three-Year Return	Five-Year Return	Ten-Year Return
11.6%	14.2%	10.0%	9.5%

Fund Performance

- Public equity program

- 64.8% of the portfolio
- returns exceeded benchmarks for the three- and five-year periods ending September 30, 2006
- underperformed performance benchmark for the fiscal year to date and one-year periods ending September 30, 2006

- Fixed income

- 19.8% of total fund
- met or exceeded performance benchmarks
- affected by inflation pressures and short-term interest rates

Fund Performance

■ Private equity

- 5.6% of total fund
- strong returns in one-, three-, and five-year periods ending September 30, 2006
- exceeded performance benchmarks
- made number of new commitments



Fund Performance

- Real estate program
 - 5% of total fund
 - strong returns in one-, three-, and five-year periods ending September 30, 2006
 - exceeded performance benchmarks
 - explored possibility of infrastructure investing

Fund Performance

■ Credit strategies program

- began on July 1, 2004
- \$2.2 billion in assets, 4.4% of total fund, as of September 30, 2006
- returned 3.5% for fiscal year and 7.2% for one-year period ending September 30, 2006
- underperformed its benchmark but expected to improve as committed assets are deployed

Recent Benefit Changes

- Legislation passed by 2005 and 2006 General Assemblies
 - Members who take military leave and return to covered positions can receive credit for their service in the armed forces
 - Monthly health insurance credit cap of \$120 removed for State employees
 - EMTs added to list of local employees for whom localities may provide retirement benefits equivalent to State Police officers
 - Retirees other than retired teachers can teach in critical shortage areas while continuing to receive retirement allowance

Research Department and Policy Changes Improve Risk Management

- Investment research department
 - conducts both basic and applied research
 - supports CIO and program directors in their portfolio management efforts
 - includes developing and employing
 - risk control methodologies
 - forward looking return estimates
 - portfolio simulations and stress testing
 - macroeconomic forecasting
 - portfolio optimization and
 - database management
- Team approach fostered by CIO and reinforced by new compensation plan
- Investment policy documents revised and clarified

Changes to Disclosure Requirements for VRS Investments Being Considered

- Freedom of Information Act (FOIA) requests for investment information increasing
- VRS has limited protection for private equity investments
- VRS' concerns relating to disclosure
 - providing advance notice of investment strategies
 - maintaining confidentiality of records relating to limited partnerships

Changes to Disclosure Requirements for VRS Investments Being Considered

- Private equity has been one of VRS' top performing asset classes
 - Access to top managers is essential for performance
 - A top private equity manager recently declined to do additional business with VRS
- VRS vetting draft legislation with FOIA Council and other stakeholders

Modernization Effort Underway

- VRS Board approved six-year modernization effort to update
 - outmoded technology systems
 - business processes
 - customer services

Modernization Effort Underway

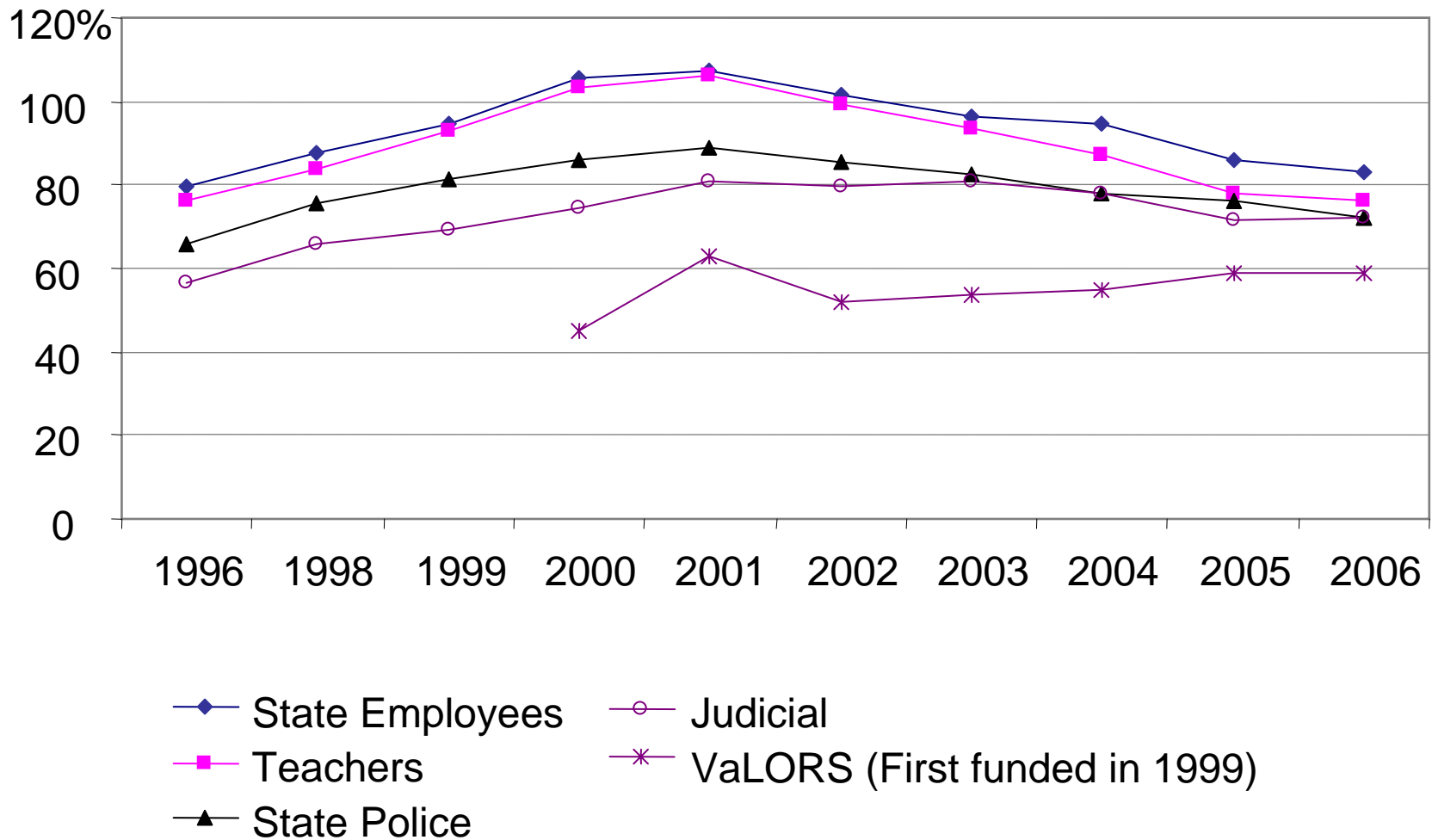
- Early initiatives include
 - myVRS online access to retirement records
 - new telephone system
 - development of RFP for IT system architecture and business process reengineering
- Replacement of the Retirement Management Information System is a priority
- Ten-year cost estimate for modernization
 - \$55 million with modernization
 - \$45 million maintaining current systems



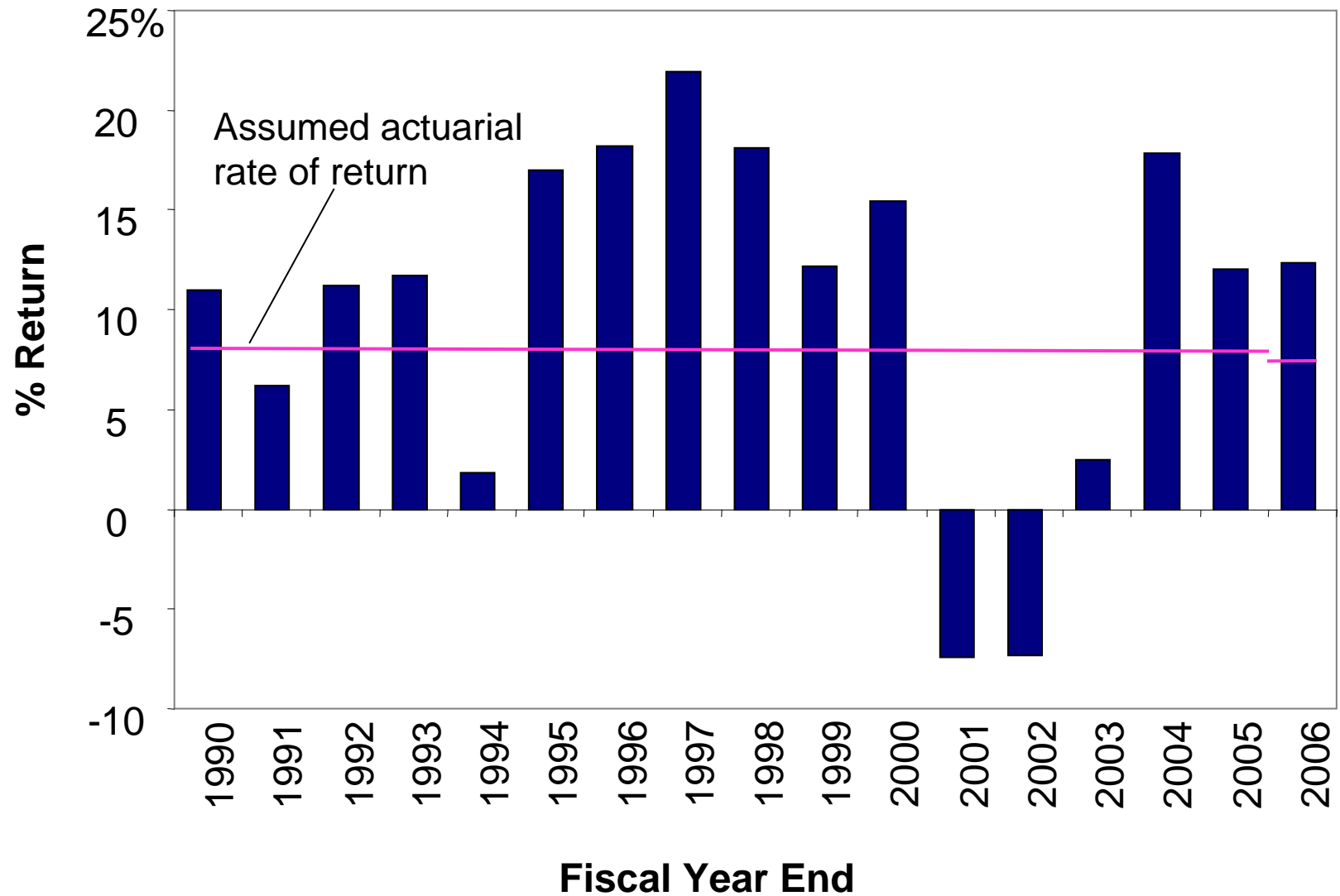
Actuarial Valuations and Benefit Funding

- 2006 actuarial valuation incorporated recommendations made in the JLARC quadrennial actuarial audit
- Pension benefits funded through combination of member contributions, employer contributions, and investment income
 - Member contribution fixed by statute at 5% of salary
 - State and most political subdivisions pay member contribution for employees
 - Employer contribution rate calculated by VRS actuary
- Separate rates calculated for State employees, teachers, State Police, other Virginia law officers, and judges
- Each political subdivision has its own contribution rate

Funded Status of the Actuarial Value of Assets



Recent VRS Annual Performance Exceeds Assumed Actuarial Rate of Return



Actuarial Valuations and Benefit Funding

- Governor and General Assembly nearly funded certified rates for FYs 2007 and 2008
- VRS actuary conducted five-year projection for State employees and teachers where
 - budgeted rates continue to be fully funded
 - all other assumptions are met
 - funded status will continue to improve

Actuarial Valuations and Benefit Funding

- Average funded ratio on the actuarial value of assets for local plans is 98.4%
 - required to fully fund actuarially determined contribution rates
 - generally have higher funded ratios than State and teacher plans
- Contribution rates for health insurance credit, group life insurance and VSDP developed on pre-funded basis under new GASB standard

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