

Virginia Retirement System

COMPREHENSIVE ANNUAL REPORT FOR THE YEAR ENDED JUNE 30, 2007

AN INDEPENDENT AGENCY OF THE COMMONWEALTH OF VIRGINIA



Virginia Retirement System
Fiscal Year 2007
Financial and Statistical Highlights – All Pension Trust Funds

(DOLLARS IN THOUSANDS)

	2007	2006	% Change
Activity for the Year			
Contributions	\$ 1,943,770	\$ 1,566,679	24.1%
Investment Income (Net of Investment Expenses)	\$ 9,753,164	\$ 5,213,323	87.1%
Retirement Benefits	\$ 2,313,489	\$ 2,101,785	10.1%
Refunds	\$ 95,765	\$ 91,230	5.0%
Administrative Expenses (Net of Miscellaneous Income)	\$ 24,190	\$ 20,166	20.0%
Increase in Net Assets Held in Trust for Pension Benefits	\$ 9,263,490	\$ 4,566,821	102.8%
Retirement Benefits as a Percentage of Contributions	119.0%	134.2%	
Retirement Benefits as a Percentage of Contributions and Investment Income	19.8%	31.0%	
Net Assets Held in Trust for Benefits at Fiscal Year End			
Virginia Retirement System (VRS)	\$ 54,948,224	\$ 46,020,734	19.4%
State Police Officers' Retirement System (SPORS)	\$ 683,949	\$ 580,371	17.8%
Virginia Law Officers' Retirement System (VaLORS)	\$ 868,366	\$ 699,923	24.1%
Judicial Retirement System (JRS)	\$ 389,664	\$ 325,685	19.6%
Investment Performance			
One-Year Return on Investments	20.4%	12.4%	
Three-Year Return on Investments	14.9%	14.0%	
Five-Year Return on Investments	12.8%	7.1%	
Participating Employers			
Counties/Cities/Towns	249	248	
Special Authorities	183	181	
School Boards	145	145	
State Agencies	237	230	
Total Employers	<u>814</u>	<u>804</u>	1.2%
Membership/Retirees			
Active Members	339,215	332,916	1.9%
Retired Members	130,500	124,639	4.7%

OUR MISSION: TO SERVE AS STEWARDS OF
THE FUNDS IN OUR CARE AND TO PROVIDE
SUPERIOR CUSTOMER SERVICE

Virginia Retirement System

COMPREHENSIVE ANNUAL FINANCIAL REPORT
FOR THE YEAR ENDED JUNE 30, 2007

AN INDEPENDENT AGENCY OF THE COMMONWEALTH OF VIRGINIA



THIS REPORT WAS PREPARED BY THE FINANCIAL, ADMINISTRATIVE AND INVESTMENT STAFF OF THE VIRGINIA RETIREMENT SYSTEM

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Virginia Retirement System

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2006

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



President

Executive Director

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Public Pension Coordinating Council
Public Pension Standards
2006 Award

Presented to

Virginia Retirement System

In recognition of meeting professional standards for
plan design and administration as
set forth in the Public Pension Standards.

Presented by the Public Pension Coordinating Council, a confederation of

National Association of State Retirement Administrators (NASRA)
National Conference on Public Employee Retirement Systems (NCPERS)
National Council on Teacher Retirement (NCTR)

A handwritten signature in cursive script that reads 'Alan H. Winkle'.

Alan H. Winkle
Program Administrator

Introductory Section

Chairman's Letter
VRS Board of Trustees
VRS Organization
VRS Investment Advisory Committee
VRS Administrative Executive Team
VRS Investment Executive Team
Professional Consultants
Letter of Transmittal



VRS will deliver the right service and the right information,
to the right customer at the right time.

"To know you is to love you." That was the analysis of results from two surveys of members and employers conducted during spring 2007. The results showed that an overwhelming majority of customers believe VRS is honest, ethical and accurate in carrying out its mission.

The Board of Trustees and the administrative and investment executive teams are proud to dedicate the *VRS Comprehensive Annual Financial Report for Fiscal Year 2007* to the more than 262 staff of VRS who commit everyday to earning customers' trust.

Chairman's Letter



Paul W. Timmreck, Chairman
Robert P. Schultze, Director
Charles W. Grant, CFA, Chief Investment Officer

P.O. Box 2500, 1200 East Main Street
 Richmond, Virginia 23218-2500
 Toll Free: 1-888-VARETIR (827-3847); TDD: (804) 344-3190

November 8, 2007

The Honorable Timothy M. Kaine, Governor of Virginia
Members of the General Assembly

I am pleased to inform you that assets of the Virginia Retirement System (VRS) fund earned 20.4% for fiscal year 2007. This return added nearly \$10 billion to the fund, which ended the year with a balance of \$58.3 billion. It also surpassed the benchmark of 18.5% for investments of the type held by the VRS Trust Fund. According to *Pensions and Investments*, VRS ranks as the nation's 26th largest public or private pension fund.

All asset classes performed well and exceeded the fund's long-term expectations. The fund's private equity and public equity investments (U.S. and international stocks) produced exceptional returns of 32.0% and 24.5%, respectively. Real estate investments generated a return of 23.8%. The fund's credit and fixed income programs contributed returns of 13.6% and 6.0%, respectively.

According to Wilshire's Trust Universe Comparison Service (TUCS) Report, VRS placed in the upper 3% of public pension funds in fiscal year 2007 returns. This outstanding result is a continuing trend for the VRS investment staff. VRS' returns for the past five years have averaged 12.85% and rank in the top 8th percentile among the TUCS peer group.

The VRS Board of Trustees expects returns to be more moderate in the years ahead. The Board, therefore, is continuing its actuarial return expectation of 7.5% in fiscal year 2008.

Your support of VRS is critical to the continued stability of the fund. The Board joins me in thanking you for your support of increased employer contribution rates approved by the 2006 and 2007 sessions of the General Assembly.

Your approval, along with the fund's investment returns, has steadied the funded status of our pension plans. Provided the Governor and General Assembly can maintain current levels of support and investment gains meet or exceed 7.5% annually, we project the funded status of the state employee plan over the next five years to improve from 85% of the assets needed to pay future benefits to 99%. The same conditions would improve the funded status of the teacher plan from 78% to 94% over the same period.

We also would like to thank you for your authorization of Senate Bill 1369, exempting sensitive investment information from the Freedom of Information Act (FOIA). Your action will protect our investment program from other investors seeking to use the trade secrets of our private investment partners to gain an unfair advantage in the financial markets, to the detriment of the VRS investment program.



“Our mission to provide financial security for members and retirees depends on knowledgeable and prudent investment management, cost-effective administration, a commitment to superior customer service and responsible Board governance. I am delighted to report that VRS posted exceptional achievements in all these areas in FY 2007.”

VRS also met significant administrative commitments in FY 2007. These included continued enhancements to the *myVRS* suite of online customer services. In February 2007, the agency launched *myVRS* for Employers. This secure online platform provides employers who are authorized to access member data an excellent tool to help them counsel their employees about VRS benefits.

In May 2007, a disability retirement estimator was added to *myVRS* and *myVRS* for Employers. This feature further expands the functions available to members and employers in a secure online environment.

In another milestone for customer service, the Customer Contact Center continued to reduce the rate of telephone calls from customers going unanswered. The abandoned call rate for FY 2007 averaged 2.0% compared to 7.3% in FY 2006 and 22% to 23% of inbound calls in previous fiscal years.

Additionally, one year after the Board of Trustees approved VRS' request to begin a long-range modernization program, VRS staff met its first-year milestones. These included several “early wins” in upgrading internal work processes and systems as well as setting the stage for the long-range implementation of the program. Please accept our thanks for your authorization this year of \$4.7 million as the first installment of VRS' six-year plan to update systems, business processes and customer services.

Our mission to provide financial security for members and retirees depends on knowledgeable and prudent investment management, cost-effective administration, a commitment to superior customer service and responsible Board governance. I am delighted to report that VRS posted exceptional achievements in all these areas in FY 2007.

On behalf of the Board of Trustees and the VRS staff, I would like to express our gratitude to you for your continued support and leadership.

Paul W. Timmreck

Chairman
Virginia Retirement System

VRS Board of Trustees



Paul W. Timmreck, Chair
Virginia
Commonwealth
University (Retired)



A. Marshall Acuff, Jr.
AMA Investment
Counsel, LLC



**John M. Albertine, Ph.D.,
Vice Chair**
Albertine Enterprises



Edwin T. Burton III, Ph.D.
University
of Virginia



J. Douglas Conway, Jr.
Henrico County
Division of Fire



Judith Ewell, Ph.D.
College of
William and Mary
(Retired)



Palmer P. Garson
Jefferson Capital Partners



Frankie D. Hughes
Hughes Capital
Management, Inc.



Raymond B. Wallace, Jr.
Henrico County Public
Schools (Retired)

Composition of the Board

Nine members serve on the VRS Board of Trustees. Their appointment is shared between the executive and legislative branches of state government.

The Governor appoints five members, including the chairman. The Joint Rules Committee of the Virginia General Assembly appoints four members. The General Assembly confirms all appointments.

Of the nine Board members, four must be investment experts; one must be experienced in employee benefit plans; one must be a local government employee; one must be an employee of a Virginia public institution of higher education; one must be a state employee; and one must be a public school teacher. The public employee members may be either active or retired.

VRS Organization

BOARD OF TRUSTEES

ADMINISTRATION



Robert P. Schultze
Director

INVESTMENTS



Charles W. Grant, CFA
Chief Investment Officer

INTERNAL AUDIT



Franklin O. Berry
Internal Audit Director

VRS Investment Advisory Committee



LEFT TO RIGHT:
*Christopher J. Brightman,
Stuart A. Sachs,
Erwin H. Will, Jr.,
Donald W. Lindsey,
Rod Smyth,
Deborah Allen-Hewitt and
Joe Grills*

NOT PICTURED:
Alice W. Handy

Joe Grills, Chair
Former Chief
Investment Officer,
IBM Retirement Funds

Christopher J. Brightman
Chief Executive Officer,
University of Virginia
Investment Management
Company

Alice W. Handy
President, Investure

Deborah Allen-Hewitt
President, Rutledge
Research

Donald W. Lindsey
Chief Investment Officer,
The George Washington
University

Stuart A. Sachs
President (Retired),
Sovran Capital Management

Rod Smyth
Chief Investment Strategist,
Wachovia Securities, LLC

Erwin H. Will, Jr., Vice Chair
Chief Investment Officer
(Retired), VRS;
President (Retired),
Capitoline Investment
Services

VRS Administrative Executive Team

Robert P. Schultze Director	Donna M. Blatecky Deputy Director, Customer Relationships Division	Barry C. Faison Chief Financial Officer
Franklin O. Berry Internal Audit Director	Craig M. Burns Director of Policy, Planning and Compliance	LaShaunda B. King Executive Assistant
L. Farley Beaton Chief Technology Officer	Jeanne L. Chenault Director of Public Relations	Kenneth C. Robertson, Jr. Director of Human Resources

VRS Investment Executive Team

Charles W. Grant, CFA Chief Investment Officer	Field H. Griffith, CFA Director of Real Estate Investment	Larry D. Kicher, CFA Chief Operations Officer
John P. Alouf, CFA Director of Private Equity	Steven C. Henderson, CFA Director of Fixed Income	Stephen R. McClelland, CFA Director of Credit Strategies
John T. Grier, CFA Director of Internal Equity	Kenneth C. Howell, CFA Director of Global Equity	Steven P. Peterson, Ph.D. Director of Research



More than 262 VRS employees commit everyday to providing the very best investment management, benefits administration, operations support and customer service on behalf of members, retirees and their employers.

Professional Consultants

ACTUARY Daniel L. Homan, EA, MAAA Senior Consultant, Wachovia Retirement Services	LIFE INSURANCE CARRIER Joseph K. W. Chang Minnesota Life Insurance Company	VIRGINIA SICKNESS & DISABILITY PROGRAM Michelle Jackson Unum Corporation
AUDITOR Walter J. Kucharski Auditor of Public Accounts, Commonwealth of Virginia	MASTER CUSTODIAN Mellon Trust	LEGAL COUNSEL Office of the Attorney General, Commonwealth of Virginia

Letter of Transmittal



Robert P. Schultze, Director
Barry C. Faison, Chief Financial Officer

P.O. Box 2500, 1200 East Main Street
Richmond, Virginia 23218-2500

Toll Free: 1-888-VARETIR (827-3847); TDD: (804) 344-3190

November 6, 2007

To the Members of the Board of Trustees:

We are pleased to submit the Comprehensive Annual Financial Report (CAFR) of the Virginia Retirement System (the “System”) for the fiscal year ended June 30, 2007.

VRS administers benefits and services for more than 582,000 members, retirees and beneficiaries covered under the following systems:

- Virginia Retirement System (VRS) for teachers, state employees and employees of participating political subdivisions, including full-time law enforcement officers, firefighters, emergency medical technicians and jail officers
- State Police Officers’ Retirement System (SPORS)
- Virginia Law Officers’ Retirement System (VaLORS)
- Judicial Retirement System (JRS)

Benefits include:

- the traditional defined benefit plan
- defined contribution plans
- the Basic Group Life Insurance Program and the Optional Group Life Insurance Program for members and retirees
- the retiree Health Insurance Credit Program
- the Virginia Sickness and Disability Program (VSDP), which includes employer-paid long-term care coverage.

More than 800 state agencies, including public colleges and universities, as well as school boards, political subdivisions and special authorities participate in VRS on behalf of their employees.

VRS’ Comprehensive Annual Report for FY 2007 has been prepared in accordance with Section 51.1-1003 of the *Code of Virginia* (1950), as amended, and Section 4-10.00 of Chapter 847 of the 2007 Virginia Acts of Assembly, which requires every retirement system to publish an annual report. The report has been mailed to the Governor and the members of his Cabinet, the members of the Virginia General Assembly, VRS’ participating employers and other interested parties. It also is available on the VRS Web site at www.varetire.org.

The FY 2007 report consists of the following sections:

- **Introductory Section:** Letter from the Chairman of the VRS Board of Trustees; Letter of Transmittal; identification of the organization.
- **Financial Section:** Opinion of the Auditor of Public Accounts; Management’s Discussion and Analysis; the financial statements and notes; required supplementary data; additional financial information.
- **Investment Section:** Letter from the Chief Investment Officer; review of investment activity and performance for the fiscal year.
- **Actuarial Section:** Certification letter of the independent consulting actuary, Wachovia Retirement Services; summary of the results of the most recent actuarial valuations; plan summary.
- **Statistical Section:** Significant data pertaining to the System; list of participating employers; information on other programs.

Accounting System and Internal Control

The financial statements included in the CAFR for FY 2007 are the responsibility of the System’s management and have been prepared in accordance with generally accepted accounting principles (GAAP) for governmental accounting and reporting under the Governmental Accounting Standards Board (GASB) and the Financial Accounting Standards Board (FASB).

The accrual basis of accounting is used in the preparation of the financial statements. Revenues are taken into account when they are earned and become measurable; expenses are recorded when the liabilities are incurred. Investments are reported at fair value as determined by the System’s master custodian. Capital assets are recorded at cost and depreciated over their estimated useful life. Contributions to the System are based on the principle of level cost funding and are developed using the entry age normal cost method with current service financed on a current basis and prior service amortized within a period of 30 years or less. In management’s opinion, the financial statements fairly present the plan net assets of the System at June 30, 2007 and the changes in its plan net assets for the period then ended.

GASB Statement Number 34 requires the System to include additional information in the CAFR. This additional information is provided in Management’s Discussion and Analysis (MD&A) and includes a narrative introduction and an overview and analysis of the System’s financial activities for the current fiscal year and the two preceding years. The Letter of Transmittal is designed to complement the MD&A and should be read in conjunction with it. The System’s MD&A can be found in the Financial Section immediately following the report of the independent auditor.

VRS Milestones	
1908	Retired Teachers Fund created.
1942	VRS created for teachers and state employees.
1944	Political subdivisions have the option to join VRS.
1950	State Police Officers’ Retirement System (SPORS) created.
1960	Group Life Insurance Program established.
1970	Cost-of-Living Adjustment (COLA) established. Judicial Retirement System (JRS) created.

VRS Milestones

- 1989** Health Insurance Credit for state retirees established.
- 1992** Health Insurance Credit for retired teachers and political subdivision retirees established.
- 1995** Optional Group Life Insurance Program established.
- 1999** Virginia Sickness and Disability Program (VSDP) for state employees established. Virginia Law Officers' Retirement System (VaLORS) created.
- 2002** Long-term care benefit added to VSDP.

The System's management is responsible for maintaining a system of adequate internal accounting controls designed to provide reasonable assurance that transactions are executed in accordance with management's general or specific authorization, and are recorded as necessary to maintain accountability for assets and to permit preparation of financial statements in accordance with GAAP. The internal control system includes the organization plan; the appropriate segregation of duties and responsibilities and sound practices in the performance of duties; and personnel with capabilities commensurate with their responsibilities. The System also conducts an internal audit program that reports to the Audit Committee of the Board of Trustees, and the budget for the System's administrative expenses is approved by the Board and appropriated by the General Assembly of Virginia.

The retirement funds held by the System are constitutionally established as independent trust funds dedicated to the exclusive benefit of its members, retirees and beneficiaries. In management's opinion, the internal controls in effect during the fiscal year ended June 30, 2007 adequately safeguard the System's assets and provide reasonable assurance regarding the proper recording of financial transactions.

Funding

The System's most recent actuarial valuation was prepared as of June 30, 2006. As expected, the report indicated a continued, but slower, rate of decline in the funded ratios for most of the plans. This decline resulted from the continuing negative impact of the investment losses in FY 2002 and a smaller investment return in FY 2003 than assumed on the Actuarial Value of Assets. Further information on this valuation is included in the Financial Section and the Actuarial Section of this CAFR.

Contributions for FY 2007 were based on the June 30, 2005 actuarial valuation. In most cases, these rates increased from the prior valuation because of the reduction in the funded ratios. For teachers and state employees, the rates certified by the VRS Board of Trustees were not fully funded by the Governor and General Assembly. The funded rates for FY 2007, however, were greater than the funded rates in FY 2006. This change is reflected in the Financial Section of the CAFR.

Investments

The VRS investment objective is to maximize the investment return while managing risk within an acceptable range. Due to the long-term nature of the plan's liabilities, the horizon for investment decisions is generally defined as 10 years or longer. Risk is assessed in an asset-liability framework. The primary risk measures are volatility in the plan's assets, funded status and contribution rates.

At June 30, 2007, the total value of the VRS investment portfolio was \$58.9 billion. This is an increase from the investment balance of \$49.2 billion at June 30, 2006. The increased growth in the portfolio resulted from an investment return of 20.4% for FY 2007, partially offset by the excess of benefit payments over contributions for the year. The System's net assets at June 30, 2007 totaled \$58.3 billion, an increase from the net asset balance of \$48.7 billion at June 30, 2006.

Legislative Initiatives

The Joint Legislative Audit and Review Commission (JLARC) launched a study to evaluate benefits for public employees in Virginia. This evaluation covers the VRS defined benefit plan, including defined contribution alternatives; law-enforcement benefits; the deferred compensation plan; disability retirement; group life insurance; and the health insurance credit.

In addition, the Virginia General Assembly enacted several bills during the 2007 session that affect public employees and retirees covered under VRS:

DEFERRED COMPENSATION PLAN

- *House Bill 1830* changed the participation in the deferred compensation plan. All classified state employees hired or re-hired on or after January 1, 2008 will automatically be enrolled in the Commonwealth of Virginia 457 Deferred Compensation Plan and given the opportunity to opt out of the plan within 90 days after the first deferral.

FREEDOM OF INFORMATION ACT (FOIA)

- *Senate Bill 1369* provided an exemption from FOIA for records containing certain sensitive investment information, including records furnished to VRS designated as trade secrets, to the extent that the disclosure of such records would have an adverse impact on the financial interest of VRS. Under an emergency enactment clause, the bill was effective March 21, 2007.

HEALTH INSURANCE CREDIT

- *House Bill 2370* and *Senate Bill 1218* increased the monthly health insurance credit from \$2.50 to \$4 for each year of service credit for teachers and school administrators who retire with at least 15 years of service credit, effective July 1, 2007. The bill also removed the health insurance credit maximum of \$75 per month for retired teachers with more than 30 years of service and changed the formula for the health insurance credit for disability retirement.

STATE AND LOCAL LAW ENFORCEMENT OFFICERS

- *Senate Bill 1166* increased the benefit multiplier from 1.7% to 1.85% for members of the State Police Officers' Retirement System (SPORS) and VRS-covered sheriffs, effective July 1, 2007. Local employers may elect to provide eligible employees the 1.85% retirement multiplier. The bill additionally requires coverage for deputy sheriffs under VRS' Enhanced Benefits for Political Subdivision Employees in Hazardous Duty Positions, effective July 1, 2008.

Year in Review

- The VRS membership grew from 562,459 in fiscal year 2006 to 582,469 in fiscal year 2007, an increase of 3.6%:
 - Active VRS members increased 1.9%, from 332,916 to 339,215.
 - Retirees and beneficiaries increased 4.7%, from 124,639 to 130,500.
 - Inactive and deferred members increased 7.5%, from 104,904 to 112,754.
- In FY 2007, the VRS retiree payroll was \$2,313,489,000, compared to \$2,101,800,000 in FY 2006.
- VRS processed more than 12,200 applications for service retirement, disability retirement and purchase of prior service during the fiscal year.
- VRS staff maintained and updated member records through processing more than 1,000 employer reports a month during the fiscal year.
- The Customer Contact Center handled more than 120,000 calls in FY 2007.
- The Member Counseling Team assisted more than 2,200 member visitors to VRS and responded to more than 4,800 e-mails during the fiscal year. Staff also conducted 112 retirement education sessions, special presentations and benefit fairs for approximately 10,600 members around the state.
- The Employer Training Team provided 18 sessions for more than 230 benefit administrators and payroll officers during FY 2007.
- VRS' Employer Representatives made more than 60 site visits and held 61 forums in locations around the state attended by more than 1,200 representatives of VRS-participating employers.
- At June 30, 2007, more than 49,000 members held active accounts through the Commonwealth of Virginia 457 Deferred Compensation Plan. Of these participants, more than 45,000 received a cash match from their employers through the Virginia Cash Match Plan.
- During FY 2007, the VRS Web site (www.varetire.org) received 995,907 visits, a 27.2% increase over the 782,582 visits logged in FY 2006. Users of *myVRS*, the secure online system launched in May 2006 for active and deferred members, helped fuel the increase in VRS Web usage.



myVRS, a secure online system for active and deferred members, continued to attract users in FY 2007.

Between July 2006 and June 2007, the number of registered members increased from 5,254 to 45,176.

VRS Accomplishments

MODERNIZATION PROGRAM

In fiscal year 2006, the Board of Trustees approved the launch of a long-range modernization program to update systems, business processes and customer services. During this fiscal year, VRS met several key first-year milestones in support of modernization:

- Achieved key “early wins” in processes and systems. These achievements included enhancements to the imaging process that supports the maintenance and updating of member records and to the Retirement Information Management System (RIMS).
- Completed the first phase of Business Process Reengineering (BPR), which entailed organizing 26 critical business processes around the three major phases of the member’s career-life cycle: “Enroll Me,” “Maintain Me” and “Benefit Me.”
- Identified more than 800 business requirements in preparation for the release of a Request for Proposals (RFP) for a modernization vendor. These requirements define the objectives and scope of a complex, multi-year program and identify what new systems must do to achieve the program’s objectives.



As a key part in developing the Modernization Program’s business requirements, VRS engaged a marketing research firm to conduct a survey of members and a survey of employers. Both surveys sought to understand customers’ current usage of VRS services and expectations for future services as well as levels of Internet access and usage.

The member survey revealed that most members are experienced Internet users. One in four respondents indicated they use *myVRS*. In addition, respondents said they would be willing to do more transactions with VRS online, including receiving benefit and retirement education, completing a retirement application and changing personal information. The survey also revealed a high level of trust in VRS, which accounted in great part for the respondents’ openness to more technology-based customer services.

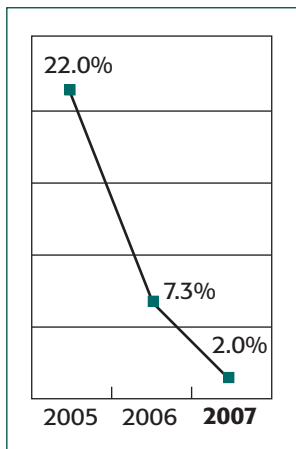
The employer survey also indicated a high level of trust in VRS. Most respondents anticipate more reliance on VRS online, self-service information, tools and other capabilities to meet their employees’ needs in the future. The information gathered from both surveys will help VRS build new channels of service for members and employers through its long-range modernization effort.

myVRS SUITE

The myVRS suite of online customer services continued to grow during the fiscal year:

- VRS staff launched myVRS for Employers in February 2007, providing employers a valuable tool to help them counsel their employees about their VRS benefits. At June 30, 2007, more than 760 employer contacts had registered for this new online system. Together, they logged more than 13,000 visits and generated almost 17,000 benefit estimates for their employees.
- In May 2007, the staff launched a disability retirement estimator in myVRS and myVRS for Employers. This function gives members who are eligible for VRS disability retirement and their employers the ability to estimate a disability benefit and further enhances the secure online functions VRS is making available to customers.

Abandoned Call Rate Reduction



The rate of calls going unanswered in FY 2007 was 2.0%. This is a decline from the abandoned call rate of 7.3% in FY 2006 and 22%-23% in previous years.

Meanwhile, member usage of myVRS climbed steadily in FY 2007. By June 2007, a year after the launch of this secure online system, more than 45,000 members had created personal myVRS online accounts, representing over 10% of eligible members. This activity matched the benchmark one-year enrollment rate of peer pension systems that support similar online systems for their members. myVRS member users logged more than 80,000 visits and generated almost 83,000 benefit estimates in FY 2007.

CUSTOMER SERVICE

The Customer Contact Center continued its progress in reducing the abandoned call rate, the rate of inbound calls that go unanswered. The abandoned call rate for FY 2007 averaged 2.0%, down from 7.3% in FY 2006 and dramatically lower than the average of 22% to 23% over previous fiscal years.

OTHER KEY AGENCY ACCOMPLISHMENTS

Among other accomplishments in fiscal year 2007, VRS staff exceeded performance standards established for business processes, such as retirement application processing and system security and availability. The agency also undertook building renovations in VRS' two downtown Richmond locations to provide better work space for the investment and customer relations support staffs.

Fiduciary Responsibility

The VRS Board of Trustees (the "Board") has full power to invest and reinvest the trust funds of the System. To fulfill its responsibility, the Board has adopted various investment policies and guidelines. The Board's investment objective for the VRS portfolio is to maximize long-term investment returns while targeting an acceptable level of risk. Primary risk measures are volatility in the plan's assets, funded status and contribution rates. As set forth in Section 11 of Article X of the Constitution of Virginia, the funds of the retirement system shall be deemed separate and independent trust funds; shall be segregated from all other funds of the Commonwealth; and shall be invested and administered solely in the interests of the members and beneficiaries thereof. The Board retains a professional investment staff, as well as outside managers, to advise and assist in the implementation of these policies and objectives.

The assets of the System are invested in a prudent manner that is intended to provide for the anticipated growth of VRS' pension liability. Section 51.1-124.30(C) of the *Code of Virginia* states that “. . . the Board shall invest the assets of the Retirement System with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with like aims.” Accordingly, the Board must sufficiently diversify the portfolio to minimize the risk of large losses unless, under the circumstances, it is clearly prudent not to do so.

Certificate of Achievement for Excellence in Financial Reporting

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the Virginia Retirement System for its comprehensive annual financial report (CAFR) for the fiscal year ended June 30, 2006. This was the 25th consecutive year that VRS achieved this prestigious recognition.

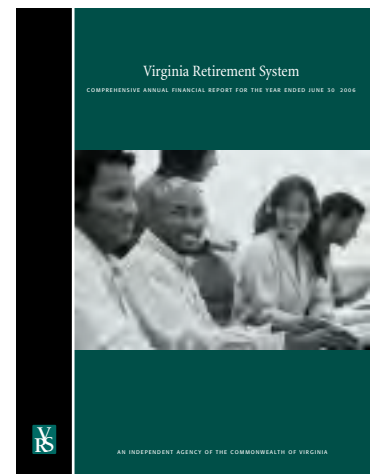
To be awarded the certificate, a government unit must publish an easily readable and efficiently organized comprehensive annual report. This report must satisfy both generally accepted accounting principles and applicable legal requirements. The certificate is valid for a period of one year only. The VRS *Comprehensive Annual Financial Report for FY 2007* continues to conform to the Certificate of Achievement Program requirements and will be submitted to GFOA to determine its eligibility for another certificate.

Achievement Award from the Public Pension Coordinating Council

VRS received the Achievement Award from the Public Pension Coordinating Council (PPCC) in recognition of the agency's excellence in meeting the Public Pension Standards. Developed by PPCC, these standards are the benchmark for measuring excellence in defined benefit plan administration. The purpose of the award is to promote high professional standards for public employee retirement systems and publicly commend systems that adhere to these standards. The PPCC is a coalition of the National Association of State Retirement Administrators (NASRA), the National Council on Teacher Retirement (NCTR) and the National Conference on Public Employee Retirement Systems (NCPERS).

Leadership Award from the National Association of Government Defined Contribution Administrators

The National Association of Government Defined Contribution Administrators (NAGDCA) awarded VRS a 2006 Leadership Award for excellence and innovation in government defined contribution plans. The award recognized VRS for expanding the scope of its Regional Education and Enrollment Meetings (REEMS) to include post-retirement strategies.



Fiscal year 2007 marked the 25th anniversary of VRS' recognition for excellence in financial reporting by the Government Finance Officers Association of the United States and Canada (GFOA).

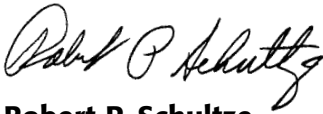
Acknowledgements

The mission of the Virginia Retirement System calls upon us to provide the best service possible and to be responsible stewards of the funds in our care on behalf of VRS members, retirees and beneficiaries. This report provides complete and reliable information that supports management's decisions in carrying out this mission.

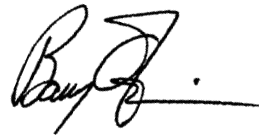
Responsible stewardship, however, is more than sound management. It also encompasses the outstanding commitment of VRS staff to excellence and the support of VRS' affiliated employers and business partners as well as the guidance and dedication of the Board of Trustees. We would like to express our sincere thanks and appreciation to each of these exceptional individuals and representatives.

Finally, we wish to thank Governor Timothy M. Kaine and the members of the Virginia General Assembly for their continued commitment to the financial security of the members and retirees of the Virginia Retirement System.

Respectfully submitted,



Robert P. Schultze
Director



Barry C. Faison
Chief Financial Officer

Financial Section

Independent Auditor's Report

Management's Discussion and Analysis

Basic Financial Statements:

Statement of Plan Net Assets

Statement of Changes in Plan Net Assets

Notes to Financial Statements

Required Supplementary Information:

Supplemental Schedule of Funding Progress –
Pension Plans

Supplemental Schedule of Employer Contributions –
Pension Plans

Notes to Required Supplemental Schedules – Pension Plans –
Actuarial Methods and Significant Assumptions

Supplemental Schedule of Funding Progress –
Other Post-Employment Benefit Plans

Notes to Required Supplemental Schedule of Funding Progress –
Other Post-Employment Benefit Plans – Actuarial Methods and
Significant Assumptions

Additional Financial Information:

Schedule of Administrative Expenses

Schedule of Professional and Consulting Services

Schedule of Investment Expenses



...the right service...

During FY 2007, VRS staff:

- Provided professional investment management of the VRS fund, which earned 20.4% for the fiscal year.
- Paid \$2.3 billion in benefits to retirees and beneficiaries.
- Reduced the rate of inbound calls going unanswered to 2% in FY 2007 from an average of 22% to 23% in previous years.
- Processed more than 12,200 applications for retirement, purchase of prior service and disability retirement.
- Launched *myVRS* for Employers, a secure online system for employers who require access to member data in order to counsel employees about their VRS benefits.
- Expanded the *myVRS* suite of online customer services with the addition of a disability retirement estimator.
- Maintained and updated member records by processing more than 1,000 employer reports each month.



Walter J. Kucharski, Auditor

Commonwealth of Virginia

Auditor of Public Accounts
P.O. Box 1295
Richmond, Virginia 23218

November 6, 2007

The Honorable Timothy M. Kaine
Governor of Virginia

The Honorable Thomas K. Norment, Jr.
Chairman, Joint Legislative Audit
And Review Commission

Board of Trustees
Virginia Retirement System

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

We have audited the accompanying basic financial statements of the Virginia Retirement System as of and for the year ended June 30, 2007 and 2006, as listed in the table of contents. These financial statements are the responsibility of the Virginia Retirement 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 and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. 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.

As discussed in Note 1, the basic financial statements of the Virginia Retirement System are intended to present the financial position and the changes in financial position of only that portion of the aggregate remaining fund information of the Commonwealth of Virginia that is attributable to the transactions of the Virginia Retirement System. They do not purport to, and do not, present fairly the Commonwealth of Virginia's overall financial position as of June 30, 2007 and 2006, and the changes in its financial position and its cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net assets of the Virginia Retirement System as of June 30, 2007 and 2006, 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.

The management's discussion and analysis, funding progress, employer contributions, and actuarial methods and significant assumptions included in the report on pages 25 through 33 and 59 through 62 are not a required part of the basic financial statements, but are supplementary information required by the accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements of the Virginia Retirement System. The introductory, investment, actuarial and statistical sections and the schedules of administrative expenses, professional and consulting services and investment expenses in the financial section are presented for the purpose of additional analysis and are not a required part of the basic financial statements. The schedules of administrative expenses, professional and consulting services and investment expenses in the financial section have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory, investment, actuarial and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

In accordance with Government Auditing Standards, we have also issued our report dated November 6, 2007 on our consideration of the Virginia Retirement 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.

AUDITOR OF PUBLIC ACCOUNTS

A handwritten signature in cursive script, appearing to read "Arthur J. Kuchanski".

Management's Discussion and Analysis (Unaudited)

The Financial Section presents Management's Discussion and Analysis of the financial statements of the Virginia Retirement System (the "System") and the significant events and conditions that affected the operations and performance of the System for the year ended June 30, 2007. We encourage readers to consider the information presented here in conjunction with the information provided in the Letter of Transmittal in the Introductory Section.

The System administers the following four defined benefit retirement plans, which are defined as pension trust funds:

- Virginia Retirement System (VRS) for state employees, teachers and public school board employees, employees of participating political subdivisions and other qualifying employees;
- State Police Officers' Retirement System (SPORS) for state police officers;
- Virginia Law Officers' Retirement System (VaLORS) for state law enforcement and correctional officers other than state police officers;
- Judicial Retirement System (JRS) for judges of state courts of record, state district courts and other qualifying employees.

The System also administers a Group Life Insurance Fund, a Retiree Health Insurance Credit Fund and a Disability Insurance Trust Fund, which are defined as other employee benefit trust funds. Both the pension and other employee benefit trust funds are classified as fiduciary funds.

Financial Highlights

- The combined total net assets held in trust for benefits of the pension trust funds increased by \$9,263.5 million, or 19.5%, during the fiscal year ended June 30, 2007. The increase was due to continued strong investment returns and higher contribution rates; however, these were partially offset by the increased expense for benefit payments.
- The System's rate of return on investments during the fiscal year ended June 30, 2007 was 20.4% compared with a return of 12.4% for the fiscal year ended June 30, 2006. The increase is primarily due to the performance of the public and private equity investments.
- The VRS, SPORS, VaLORS and JRS plans were actuarially funded at 80.8%, 73.8%, 59.9% and 71.3% based on the actuarial valuation as of June 30, 2006. For the VRS, SPORS and JRS plans, this was a decline from their funded ratios of 81.3%, 76.4% and 71.5% based on the actuarial valuation as of June 30, 2005. For the VaLORS plan, there was a slight improvement from the June 30, 2005 funded ratio of 58.7%. There were no changes in the primary actuarial assumptions for the investment rate of return or inflation. However, the funded ratios continue to reflect the impact of the significant investment losses recorded in FY 2001 and FY 2002 on the Actuarial Value of Assets because of the "five-year smoothing" asset valuation method used by the VRS actuary.

Overview of the Financial Statements and Accompanying Information

1. **FUND FINANCIAL STATEMENTS.** The System presents the Statement of Plan Net Assets as of June 30, 2007 and 2006 and the Statement of Changes in Plan Net Assets for the years then ended. The statements were prepared on the accrual basis of accounting and are used to account for resources administered by VRS for the benefit of the plan members and beneficiaries. These statements include:
 - Statement of Plan Net Assets – Defined Benefit Pension Trust Funds and Other Employee Benefit Trust Funds. This statement reflects the balance of the resources available to pay benefits to members, including retirees and beneficiaries, at the end of the fiscal year.
 - Statement of Changes in Plan Net Assets – Defined Benefit Pension Trust Funds and Other Employee Benefit Trust Funds. This statement reflects the changes in the resources available to pay benefits to members, including retirees and beneficiaries, during the fiscal year.
2. **NOTES TO FINANCIAL STATEMENTS.** The Notes to Financial Statements are an integral part of the financial statements and contain additional detailed information and schedules to provide a better understanding of the financial statements.
3. **REQUIRED SUPPLEMENTARY INFORMATION – PENSION PLANS.** The required supplementary information consists of:
 - Required Supplemental Schedule of Funding Progress – Pension Plans
 - Required Supplemental Schedule of Employer Contributions – Pension Plans
 - Notes to Required Supplemental Schedules – Pension Plans – Actuarial Methods and Significant Assumptions
4. **REQUIRED SUPPLEMENTARY INFORMATION – OTHER POST-EMPLOYMENT BENEFITS (OPEB).** The required supplementary information consists of:
 - Required Supplemental Schedule of Funding Progress – Other Post-Employment Benefits
 - Notes to Required Supplemental Schedule – Other Post-Employment Benefits – Actuarial Methods and Significant Assumptions
5. **OTHER SUPPLEMENTARY SCHEDULES.** The following supplementary schedules provide additional details not included in the basic financial statements:
 - Schedule of Administrative Expenses
 - Schedule of Professional and Consulting Services
 - Schedule of Investment Expenses

Plan Net Assets

(EXPRESSED IN MILLIONS)

	2007	Increase (Decrease)	2006	Increase (Decrease)	2005
Assets					
Cash, Receivables and Capital Assets	\$ 3,782.6	\$ 1,339.1	\$ 2,443.5	\$ (249.3)	\$ 2,692.8
Investments	59,883.1	10,696.3	49,186.8	4,337.3	44,849.5
Security Lending Collateral	5,740.4	1,721.4	4,019.0	(166.7)	4,185.7
Total Assets	\$ 69,406.1	\$ 13,756.8	\$ 55,649.3	\$ 3,921.3	\$ 51,728.0
Liabilities					
Accounts Payable	\$ 177.5	\$ (212.0)	\$ 389.5	\$ 145.4	\$ 244.1
Investment Purchases Payable	5,147.5	2,654.7	2,492.8	(682.5)	3,175.3
Obligations Under Security Lending	5,740.4	1,721.4	4,019.0	(166.7)	4,185.7
Total Liabilities	\$ 11,065.4	\$ 4,164.1	\$ 6,901.3	\$ (703.8)	\$ 7,605.1
Total Net Assets	\$ 58,340.7	\$ 9,592.7	\$ 48,748.0	\$ 4,625.1	\$ 44,122.9

Changes in Plan Net Assets

(EXPRESSED IN MILLIONS)

	2007	Increase (Decrease)	2006	Increase (Decrease)	2005
Additions					
Member Contributions	\$ 132.3	\$ 92.5	\$ 39.8	\$ (25.1)	\$ 64.9
Member Contributions Paid by Employer	703.9	42.9	661.0	39.5	621.5
Employer Contributions	1,436.0	425.2	1,010.8	92.5	918.3
Net Investment Income	9,989.0	4,648.4	5,340.6	621.1	4,719.5
Total Additions	\$ 12,261.2	\$ 5,209.0	\$ 7,052.2	\$ 728.0	\$ 6,324.2
Liabilities					
Retirement Benefits	\$ 2,313.5	\$ 211.7	\$ 2,101.8	\$ 156.3	\$ 1,945.5
Refunds of Member Contributions	95.8	4.6	91.2	6.5	84.7
Insurance Premiums and Claims	118.6	7.1	111.5	14.4	97.1
Retiree Health Insurance Credit Reimbursements	80.4	7.9	72.5	3.5	69.0
Disability Insurance Benefits	33.3	6.0	27.3	1.5	25.8
Administrative and Other Expenses	26.9	4.1	22.8	1.8	21.0
Total Deductions	\$ 2,668.5	\$ 241.4	\$ 2,427.1	\$ 184.0	\$ 2,243.1
Net Increase (Decrease) in Net Assets	\$ 9,592.7	\$ 4,967.6	\$ 4,625.1	\$ 544.0	\$ 4,081.1

Analysis of Financial Activities – Pension Plans

The System's funding objective is to meet its long-term benefit obligations through investment income and contributions. Accordingly, the collection of contributions and the income from investments provide the reserves needed to finance the benefits provided under the plans.

MEMBERSHIP

As discussed earlier, the System administers retirement plans for a variety of employee groups. The distribution of the active membership as of June 30, 2007, 2006 and 2005 is presented in Figure 1.

FIGURE 1.
Active Membership Distribution at June 30

	2007	2006	2005
State Employees (VRS)	80,262	79,728	78,158
Teachers (VRS)	145,122	142,467	139,209
Political Subdivision Employees (VRS)	101,461	98,690	95,658
State Police Officers (SPORS)	1,885	1,790	1,807
Virginia Law Officers (VaLORS)	10,061	9,826	9,779
Judges (JRS)	424	415	414
Total	<u>339,215</u>	<u>332,916</u>	<u>325,025</u>

CONTRIBUTIONS AND INVESTMENT EARNINGS

Pension trust fund revenue is used to finance the retirement benefits provided by the retirement plans. The primary sources of revenue for the retirement plans include contributions from active members and their employers, as well as investment income generated from the investment of plan assets. Total contributions and investment earnings for the fiscal year ended June 30, 2007 amounted to \$11,697.4 million. This was an increase of \$4,917.0 million when compared with FY 2006 and also an increase from the gain of \$710.5 million that was recorded in FY 2006. This information is presented in Figure 2.

Total member contributions, including those paid by employers, increased \$33.3 million, while employer contributions increased \$343.8 million for a total increase in contributions of \$377.1 million from the previous fiscal year. Investment income also provided a significant increase to plan net assets in FY 2007. Member contributions paid by members decreased by \$9.6 million. This was caused mostly by a continuing decline in activity among members purchasing previously refunded and other qualified service. Employer contributions increased primarily due to some payroll growth; an increase in the employer contribution rates for most employer groups as a result of the June 30, 2005 actuarial valuation; and the addition of special coverage by some local governments. This is discussed further in Note 14 of the Notes to Financial Statements. During FY 2006, the System experienced growth in total member contributions of \$14.5 million and an increase in employer contributions of \$84.0 million. As in FY 2007, the member contributions were affected by the number of members purchasing service. The growth in employer contributions is related to payroll growth, the addition of some new local government employers and the addition of enhanced hazardous duty or other coverage by some local governments.

FIGURE 2.
Contributions and Investment Earnings for the Years Ended June 30

(EXPRESSED IN MILLIONS)

	2007	Increase (Decrease)	2006	Increase (Decrease)	2005
Member Contributions	\$ 30.2	\$ (9.6)	\$ 39.8	\$ (25.0)	\$ 64.8
Member Contributions Paid by Employer	703.9	42.9	661.0	39.5	621.5
Employer Contributions	1,209.7	343.8	865.9	84.0	781.9
Net Investment Income *	9,753.6	4,539.9	5,213.7	612.0	4,601.7
Total	\$ 11,697.4	\$ 4,917.0	\$ 6,780.4	\$ 710.5	\$ 6,069.9

* Net of investment expenses, including net securities lending income and miscellaneous income.

INVESTMENTS

There was net investment income for FY 2007 of \$9,753.6 million, which represented an increase of \$4,539.9 million from FY 2006 (Figure 2). This compares to a net investment income increase of \$612.0 million in FY 2006. Total pension trust fund investments increased to \$58,371.7 million at fair value at June 30, 2007. This was an increase of \$10,345.3 million over the fair value of \$48,026.4 million at June 30, 2006. The total pension trust fund investments also increased in FY 2006 by \$4,283.2 million from their fair value of \$43,743.2 million at June 30, 2005.

The total return on pension trust fund investments for the fiscal year ended June 30, 2007 was 20.4%. The annualized return was 14.9% over the past three years and 12.8% over the past five years. An explanation of investment policies and strategies and the portfolio's composition is included in the Investment Section of this CAFR. A review of investment activity and results for FY 2007 also is provided in that section.

The System's investment portfolio consists of funds contributed by both employers and employees of Virginia's state agencies, teachers, state police, other law enforcement officers and participating local governments. These contributions are held in a commingled pool and invested to provide for the payment of current and future benefits to participants when they retire. Each plan owns an equity position in the pool and receives a proportionate share of the total investment income or loss from the pool.



The System's funding objective is to meet its long-term benefit obligations through investment income and contributions.

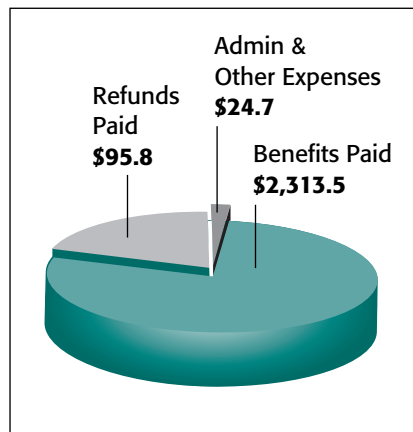
FIGURE 3.
Primary Expenses for the Years Ended June 30

(EXPRESSED IN MILLIONS)

	2007	Increase (Decrease)	2006	Increase (Decrease)	2005
Benefits	\$ 2,313.5	\$ 211.7	\$ 2,101.8	\$ 156.3	\$ 1,945.5
Refunds	95.8	4.6	91.2	6.5	84.7
Administrative and Other Expenses	24.7	4.1	20.6	1.7	18.9
Total	\$ 2,434.0	\$ 220.4	\$ 2,213.6	\$ 164.5	\$ 2,049.1

Pension Plan Activity –
Fiscal Year 2007

(EXPRESSED IN MILLIONS)



EXPENSES—DEDUCTIONS FROM PLAN NET ASSETS

The primary expenses of the pension trust funds include annuity benefits for retirees and beneficiaries; refunds of contributions to former members; and expenses associated with the administration of the retirement plans. Expenses for FY 2007 totaled \$2,434.0 million, an increase of \$220.4 million, or 10.0%, over the 2006 period. The details are presented in Figure 3.

The increase in benefit payments to \$2,313.5 million in FY 2007 was due to continued growth in the number of retirees and beneficiaries receiving benefits combined with a cost-of-living adjustment (COLA) of 3.2% on July 1, 2006. The number of retirees and beneficiaries receiving benefit payments was approximately 130,500 at June 30, 2007, an increase of 4.7% from the 124,639 retirees and beneficiaries at June 30, 2006. The increase in benefit payments for FY 2007 was \$211.7 million compared to \$156.3 million for FY 2006.

Refunds of contributions to members who terminated employment during FY 2007 amounted to \$95.8 million (13,586 refunds), compared with \$91.2 million refunded (14,139 refunds) during FY 2006 and \$84.7 million refunded (13,588 refunds) during FY 2005. The change during FY 2007 reflects a higher average refund amount compared to FY 2006.

Administration and other expenses for FY 2007 were \$24.7 million, compared with \$20.6 million for FY 2006 and \$18.9 million for FY 2005. Administration expenses increased \$4.1 million for FY 2007. This compares to an increase in administration expenses in FY 2006 of \$1.7 million. The increase is related to benefit costs, as well as other administrative costs. Further details are provided in the Schedule of Administrative Expenses.

RETIREMENT RESERVES

Funds are accumulated by the pension plans to meet current and future obligations to retirees and beneficiaries and are derived from the excess of revenues over expenses. The higher the level of funding, the larger the accumulation of assets and the greater the investment income potential.

Since revenues exceeded expenses for FY 2007, there was a net increase of \$9,263.5 million in the retirement reserves held by the plans. This compares to an increase of \$4,566.9 million in the retirement reserves in FY 2006. As noted above, the increase for FY 2007 was primarily related to the investment performance for the year, which was significantly higher than in FY 2006. During the fiscal year, the amount of interest credited to member accounts was \$673.9 million. The amount of member balances transferred to employer reserves upon members' retirements was \$446.5 million. The member and employer balances in retirement reserves at June 30, 2007 are presented in Figure 4.

ACTUARIAL VALUATIONS AND FUNDING PROGRESS

The System's actuarial firm performs actuarial valuations of VRS, SPORS, VaLORS and JRS at least every two years to determine funding requirements. The funding policy provides for periodic employer contributions at actuarially determined rates that will remain relatively level over time as a percentage of payroll and will accumulate sufficient assets to meet the costs of all basic benefits when due.

The latest valuations of the four pension plans performed as of June 30, 2006 by the VRS consulting actuary, Wachovia Retirement Services, indicated that the ratio of assets accumulated by the plans to their total actuarial accrued liabilities for benefits was 80.8% for VRS, 73.8% for SPORS, 59.9% for VaLORS and 71.3% for JRS. The valuations reflect full pre-funding of the statutory cost-of-living adjustment (COLA) for retirees. Funding progress for the pension plans is presented in the Required Supplemental Schedule of Funding Progress – Pension Plans. Additional information on the plans' funding progress is presented in the Actuarial Section of this CAFR.

FIGURE 4.
Reserve Balances at June 30

(EXPRESSED IN MILLIONS)

	2007	Increase (Decrease)	2006	Increase (Decrease)	2005
Member Reserves	\$ 9,116.7	\$ 1,198.7	\$ 7,918.0	\$ 519.2	\$ 7,398.8
Employer Reserves	47,773.5	8,064.8	39,708.7	4,047.7	35,661.0
Total	\$ 56,890.2	\$ 9,263.5	\$ 47,626.7	\$ 4,566.9	\$ 43,059.8

Analysis of Financial Activities – Other Employee Benefit Plans

GROUP AND OPTIONAL LIFE INSURANCE PROGRAMS

The group life insurance program, enacted by the Virginia General Assembly on July 1, 1960, provides life insurance and accidental death and dismemberment coverage to the majority of members covered under the pension plans administered by the System as well as other qualifying employees. Group life insurance premiums are paid by covered employees and/or employers to fund the program. Approximately 355,046 members and 122,947 retirees were covered by the group life insurance program at June 30, 2007.

During FY 2007, the System remitted \$118.6 million to the insurance company for claims and administrative costs. This is an increase from the \$111.5 million remitted for FY 2006. The difference between the amounts collected and paid by the System for the group life insurance program is added to the reserve established to pre-fund death benefits for retirees. This reserve had net assets held in trust for benefits of \$962.3 million at June 30, 2007 and an investment income, including net securities lending income, of \$160.9 million during the fiscal year. For FY 2006, this reserve had an investment income of \$92.2 million and ended the year with a reserve balance of \$751.4 million, down from the \$771.8 million at June 30, 2005. For FY 2007, the growth is the result of investment income and the resumption of contributions after the premium holiday declared by the General Assembly beginning in April 2002.

The optional life insurance program, enacted by the General Assembly on November 1, 1995, provides life insurance and accidental death and dismemberment coverage to members covered under the group life insurance program as a supplement to that program. Members also may cover their spouses and children under this program. Optional life insurance premiums are paid by the members. There were approximately 60,820 members participating in the program at June 30, 2007. This compares to approximately 61,508 members participating in the program at June 30, 2006.

RETIREE HEALTH INSURANCE CREDIT PROGRAM

The retiree health insurance credit program was established by the General Assembly on January 1, 1990 to provide credits against health insurance premiums for eligible state retirees. Coverage under the program was extended to retired teachers and employees of participating political subdivisions on July 1, 1993. During FY 2007, the System collected \$92.9 million in retiree health insurance credit contributions from participating employers and provided reimbursements of \$80.4 million to 76,119 eligible retirees. During FY 2006, the System collected \$86.9 million in retiree health insurance credit contributions from participating employers and provided reimbursements of \$72.5 million to approximately 72,387 eligible retirees. The growth in contributions reflects a continuation of general payroll increases and an increase in contribution rates. The growth in retiree health insurance credits reflects the increase in the number of eligible retirees. The Retiree Health Insurance Credit Fund reserve had net assets held in trust for benefits of \$224.6 million at June 30, 2007 and an investment income, including net securities lending income, of \$34.4 million during the fiscal year. The reserve balances at June 30, 2006 and June 30, 2005 were \$178.1 million and \$147.0 million, respectively.

VIRGINIA SICKNESS AND DISABILITY PROGRAM

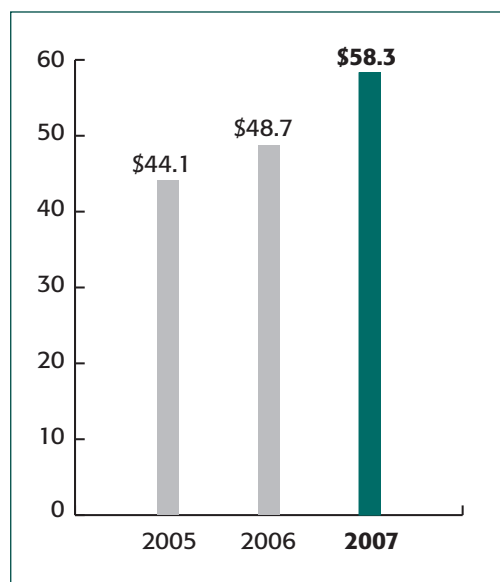
The Disability Insurance Trust Fund, also known as the Virginia Sickness and Disability Program (VSDP), was established by the General Assembly on January 1, 1999 and provides sick, family and personal leave and short-term and long-term disability benefits to eligible state employees. The System is responsible for the administration of the program and the payment of long-term disability benefits. Sick leave and short-term disability benefits are paid to eligible employees by their employers. During FY 2007, the System collected \$65.7 million in VSDP contributions from participating employers and provided long-term disability benefits of \$33.3 million to eligible members. This is an increase over the \$58.0 million in contributions collected and \$27.3 million in benefits paid in FY 2006. Contribution increases reflect growth in covered payrolls and an increase in the contribution rate. The increase in benefits reflects growth in the number of members receiving long-term disability benefits, the amount of these benefits and the operating costs of the program. The Disability Insurance Trust Fund reserve had net assets held in trust for benefits of \$263.6 million at June 30, 2007 and an investment income, including net securities lending income, of \$40.0 million during the fiscal year. The reserve balances at June 30, 2006 and June 30, 2005 were \$191.9 million and \$144.2 million, respectively.

REQUEST FOR INFORMATION

This financial report is designed to provide a general overview of the Virginia Retirement System’s finances. Questions concerning the information provided in this report or requests for additional information should be addressed to the Chief Financial Officer of the Virginia Retirement System, P.O. Box 2500, Richmond, VA 23218-2500.

System Net Assets

(BILLIONS OF DOLLARS)



Virginia Retirement System Statement of Plan Net Assets – Defined Benefit Pension Trust Funds and Other Employee Benefit Trust Funds

AS OF JUNE 30, 2007 AND 2006
(EXPRESSED IN THOUSANDS)

	Pension Trust Funds				
	Virginia Retirement System	State Police Officers' Retirement System	Virginia Law Officers' Retirement System	Judicial Retirement System	Total Pension Trust Funds
Assets					
Cash (Note 6)	\$ 71,738	\$ 806	\$ 1,022	\$ 459	\$ 74,025
Receivables:					
Contributions	151,563	919	2,879	999	156,360
Interest and Dividends	169,745	2,114	2,679	1,203	175,741
Receivable for Security Transactions	3,090,492	38,486	48,773	21,895	3,199,646
Other Receivables	33,865	408	516	249	35,038
Total Receivables	3,445,665	41,927	54,847	24,346	3,566,785
Due from Other Funds	4,899	2,847	3,071	2,097	12,914
Investments (Note 6)					
Bonds and Mortgage Securities	14,041,722	174,864	221,601	99,479	14,537,666
Stocks	22,762,761	283,469	359,233	161,263	23,566,726
Fixed Income Commingled Funds	1,175,237	14,636	18,547	8,326	1,216,746
Index and Pooled Funds	11,916,499	148,398	188,062	84,422	12,337,381
Real Estate	2,432,685	30,295	38,392	17,234	2,518,606
Private Equity	3,467,052	43,176	54,716	24,562	3,589,506
Short-Term Investments	584,457	7,278	9,224	4,141	605,100
Total Investments	56,380,413	702,116	889,775	399,427	58,371,731
Collateral on Loaned Securities	5,404,650	67,305	85,294	38,289	5,595,538
Property, Plant, Furniture and Equipment (Note 7)	6,434	–	–	–	6,434
Total Assets	65,313,799	815,001	1,034,009	464,618	67,627,427
Liabilities					
Retirement Benefits Payable	48,691	2,778	2,819	2,060	56,348
Refunds Payable	7,227	140	327	–	7,694
Accounts Payable and Accrued Expenses	39,950	475	602	270	41,297
Compensated Absences Payable	1,620	–	–	–	1,620
Insurance Premiums and Claims Payable	–	–	–	–	–
Payable for Security Transactions	4,846,401	60,353	76,484	34,334	5,017,572
Other Payables	1,790	1	1	1	1,793
Obligations Under Security Lending Program	5,404,650	67,305	85,294	38,289	5,595,538
Due to Other Funds	15,246	–	116	–	15,362
Total Liabilities	10,365,575	131,052	165,643	74,954	10,737,224
Net Assets Held in Trust for Benefits (Note 5)					
(See Required Supplemental Schedule of Funding Progress)	\$54,948,224	\$ 683,949	\$ 868,366	\$ 389,664	\$56,890,203

The accompanying Notes to Financial Statements are an integral part of this statement.

Other Employee Benefit Trust Funds				Totals	
Group Life Insurance Fund	Retiree Health Insurance Credit Fund	Disability Insurance Trust Fund	Total Other Employee Benefit Trust Funds	2007	2006
\$ 1,163	\$ 260	\$ 312	\$ 1,735	\$ 75,760	\$ 237,913
12,931	6,470	2,830	22,231	178,591	115,209
3,050	681	819	4,550	180,291	141,595
55,532	12,407	14,907	82,846	3,282,492	1,842,223
586	144	2,902	3,632	38,670	84,086
72,099	19,702	21,458	113,259	3,680,044	2,183,113
1,000	6,494	–	7,494	20,408	15,632
252,309	56,370	67,731	376,410	14,914,076	10,451,767
409,013	91,380	109,799	610,192	24,176,918	16,377,422
21,117	4,718	5,669	31,504	1,248,250	2,166,851
214,122	47,838	57,481	319,441	12,656,822	14,501,774
43,712	9,766	11,734	65,212	2,583,818	1,524,935
62,298	13,918	16,724	92,940	3,682,446	2,708,592
10,502	2,346	2,819	15,667	620,767	1,455,460
1,013,073	226,336	271,957	1,511,366	59,883,097	49,186,801
97,113	21,697	26,070	144,880	5,740,418	4,019,013
–	–	–	–	6,434	6,780
1,184,448	274,489	319,797	1,778,734	69,406,161	55,649,252
–	–	–	–	56,348	178,985
1,761	234	24	2,019	9,713	6,102
687	7,058	5,928	13,673	54,970	152,628
–	–	–	–	1,620	1,410
32,678	–	–	32,678	32,678	30,943
87,083	19,456	23,377	129,916	5,147,488	2,492,766
2	–	–	2	1,795	3,759
97,113	21,697	26,070	144,880	5,740,418	4,019,013
2,796	1,438	812	5,046	20,408	15,632
222,120	49,883	56,211	328,214	11,065,438	6,901,238
\$ 962,328	\$ 224,606	\$ 263,586	\$ 1,450,520	\$ 58,340,723	\$ 48,748,014

Virginia Retirement System Statement of Changes in Plan Net Assets – Defined Benefit Pension Trust Funds and Other Employee Benefit Trust Funds

FOR THE YEARS ENDED JUNE 30, 2007 AND 2006
(EXPRESSED IN THOUSANDS)

	Pension Trust Funds				Total Pension Trust Funds
	Virginia Retirement System	State Police Officers' Retirement System	Virginia Law Officers' Retirement System	Judicial Retirement System	
Additions					
Contributions:					
Members	\$ 29,489	\$ 213	\$ 371	\$ 92	\$ 30,165
Member-Paid by Employers	680,023	4,895	16,127	2,815	703,860
Employers	1,124,535	16,358	48,322	20,530	1,209,745
Total Contributions	1,834,047	21,466	64,820	23,437	1,943,770
Investment Income					
Net Appreciation/(Depreciation) in Fair Value of Investments	8,308,270	103,567	126,628	58,143	8,596,608
Interest, Dividends and Other Investment Income	1,341,897	16,728	20,453	9,391	1,388,469
Total Investment Income Before Investment Expenses	9,650,167	120,295	147,081	67,534	9,985,077
Investment Expenses	(239,052)	(2,980)	(3,644)	(1,674)	(247,350)
Net Investment Income	9,411,115	117,315	143,437	65,860	9,737,727
Security Lending Income:					
Gross Income	260,548	3,248	3,971	1,823	269,590
Less Borrower Rebates and Agent Fees	(245,628)	(3,062)	(3,744)	(1,719)	(254,153)
Net Security Lending Income	14,920	186	227	104	15,437
Miscellaneous Revenue	338	-	-	-	338
Transfers In	-	-	171	-	171
Total Additions	11,260,420	138,967	208,655	89,401	11,697,443
Deductions					
Retirement Benefits	2,219,350	33,867	35,019	25,253	2,313,489
Refunds of Member Contributions	89,716	1,221	4,828	-	95,765
Insurance Premiums and Claims	-	-	-	-	-
Retiree Health Insurance Credit Reimbursements	-	-	-	-	-
Disability Insurance Benefits	-	-	-	-	-
Administrative Expenses	23,686	301	365	169	24,521
Other Expenses	7	-	-	-	7
Transfers Out	171	-	-	-	171
Total Deductions	2,332,930	35,389	40,212	25,422	2,433,953
Net Increase (Decrease)	8,927,490	103,578	168,443	63,979	9,263,490
Net Assets Held in Trust for Benefits - Beginning of Year	46,020,734	580,371	699,923	325,685	47,626,713
Net Assets Held in Trust for Benefits - End of Year	\$ 54,948,224	\$ 683,949	\$ 868,366	\$ 389,664	\$56,890,203

The accompanying Notes to Financial Statements are an integral part of this statement.

Other Employee Benefit Trust Funds				Totals	
Group Life Insurance Fund	Retiree Health Insurance Credit Fund	Disability Insurance Trust Fund	Total Other Employee Benefit Trust Funds	2007	2006
\$ 102,194	\$ -	\$ -	\$ 102,194	\$ 132,359	\$ 39,803
-	-	-	-	703,860	661,014
67,630	92,919	65,726	226,275	1,436,020	1,010,818
<u>169,824</u>	<u>92,919</u>	<u>65,726</u>	<u>328,469</u>	<u>2,272,239</u>	<u>1,711,635</u>
141,803	30,340	35,287	207,430	8,804,038	4,497,554
<u>22,903</u>	<u>4,900</u>	<u>5,700</u>	<u>33,503</u>	<u>1,421,972</u>	<u>1,062,674</u>
164,706	35,240	40,987	240,933	10,226,010	5,560,228
(4,080)	(872)	(1,015)	(5,967)	(253,317)	(237,707)
<u>160,626</u>	<u>34,368</u>	<u>39,972</u>	<u>234,966</u>	<u>9,972,693</u>	<u>5,322,521</u>
4,447	951	1,107	6,505	276,095	179,944
(4,192)	(897)	(1,043)	(6,132)	(260,285)	(162,375)
<u>255</u>	<u>54</u>	<u>64</u>	<u>373</u>	<u>15,810</u>	<u>17,569</u>
-	-	-	-	338	185
-	-	-	-	171	255
<u>330,705</u>	<u>127,341</u>	<u>105,762</u>	<u>563,808</u>	<u>12,261,251</u>	<u>7,052,165</u>
-	-	-	-	2,313,489	2,101,785
-	-	-	-	95,765	91,230
118,627	-	-	118,627	118,627	111,490
-	80,447	-	80,447	80,447	72,482
-	-	33,282	33,282	33,282	27,339
568	356	766	1,690	26,211	21,977
543	-	-	543	550	492
-	-	-	-	171	255
<u>119,738</u>	<u>80,803</u>	<u>34,048</u>	<u>234,589</u>	<u>2,668,542</u>	<u>2,427,050</u>
210,967	46,538	71,714	329,219	9,592,709	4,625,115
<u>751,361</u>	<u>178,068</u>	<u>191,872</u>	<u>1,121,301</u>	<u>48,748,014</u>	<u>44,122,899</u>
<u>\$ 962,328</u>	<u>\$ 224,606</u>	<u>\$ 263,586</u>	<u>\$ 1,450,520</u>	<u>\$58,340,723</u>	<u>\$ 48,748,014</u>

Notes to Financial Statements

JUNE 30, 2007 AND 2006

1. Summary of Significant Accounting Policies

A. FINANCIAL REPORTING ENTITY

The Virginia Retirement System (the “System”) is an independent agency of the Commonwealth of Virginia that administers defined benefit pension plans, other employee benefit plans and other funds established by the Commonwealth. The System is included in the basic financial statements of the Commonwealth of Virginia. As required by generally accepted accounting principles (GAAP), these financial statements include all of the funds for which financial transactions are recorded in the System’s accounting system and for which its Board of Trustees exercises administrative responsibility.

Defined Benefit Pension Plans

Virginia Retirement System (VRS)
State Police Officers’ Retirement System (SPORS)
Virginia Law Officers’ Retirement System (VaLORS)
Judicial Retirement System (JRS)

Other Employee Benefit Plans

Group Life Insurance Fund
Retiree Health Insurance Credit Fund
Disability Insurance Trust Fund (also known as the Virginia Sickness and Disability Program [VSDP])

Effective January 1, 1997, the Constitution of Virginia was amended to strengthen the independence of the Virginia Retirement System and to protect its funds by requiring that they be separate and independent trust funds segregated from all other funds of the Commonwealth and administered solely in the interest of the members and beneficiaries thereof.

B. ADMINISTRATION

The Board of Trustees is responsible for the general administration and operation of the defined benefit pension plans, other employee benefit plans and other funds. The Board consists of five members appointed by the Governor and four members appointed by the Joint Rules Committee, all subject to confirmation by the General Assembly of Virginia. The Board of Trustees 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. Full power to invest and reinvest the assets of the defined benefit pension plans, other employee benefit plans and other funds is vested in the Board. The Board of Trustees has appointed Mellon Trust as the custodian of designated assets of the System.

The Virginia Retirement System, the State Police Officers’ Retirement System, the Virginia Law Officers’ Retirement System and the Judicial Retirement System are administered in accordance with Title 51.1, Chapters 1, 2, 2.1, 3 and 4 of the *Code of Virginia* (1950), as amended. The Group Life Insurance Fund, the Retiree Health Insurance Credit Fund and the

Disability Insurance Trust Fund are administered in accordance with Title 51.1, Chapter 5; Title 51.1, Chapter 14; and Title 51.1, Chapter 11, respectively, of the *Code of Virginia* (1950), as amended.

The Optional Life Insurance Fund is administered in accordance with Sections 51.1-512 and 51.1-512.1 of the *Code of Virginia* (1950), as amended. Because optional life insurance is an insured product and the premium collection is handled by the carrier, the Board of Trustees provides only oversight for the program with little administrative responsibility.

The Board of Trustees has oversight responsibility, but little administrative involvement and no investment responsibility, for the following: the Commonwealth's Deferred Compensation Plan (IRC Section 457) and its Cash Match Plan for state employees and employees of participating political subdivisions; defined contribution plans for political appointees, employees of public institutions of higher education and certain employees of public school divisions and teaching hospitals; the Commonwealth Health Research Fund, which provides financial support for research efforts that may maximize human health benefits for citizens of the Commonwealth; and the Volunteer Firefighters' and Rescue Squad Workers' Service Award Fund, which provides service awards to eligible volunteer firefighters and rescue squad workers. Because the Board of Trustees neither owns the assets nor has custody of them, and their financial transactions are not recorded in the System's accounting system, these programs are not included in the System's financial statements.

C. BASIS OF ACCOUNTING

The accounts of the defined benefit pension plans and other employee benefit plans are accounted for and presented using the flow of economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recognized when liabilities are incurred, regardless of the timing of related cash flows. Member and employer contributions are recognized as revenues when due, pursuant to formal commitments as well as statutory or contractual requirements; and investment income is recognized as earned by the plans. Benefits and refunds are recognized when due and payable in accordance with the terms of the plans.

D. INVESTMENTS

1. Investment Valuation

Investments are reported at fair value as determined by the System's master custodian, Mellon Trust, from its Global Pricing System. This system assigns a price source, based on asset type and the vendor pricing products to which the master custodian subscribes, for every security held immediately following its acquisition. Prices supplied by these sources are monitored daily by the master custodian.

When a pricing source is unable to provide a price, quotes are sought from major investment brokers and market-making dealers; or internal calculations are applied, if feasible. As a last resort, the master custodian will contact investment managers for a price. Commingled funds, partnerships and real estate assets are priced by the master custodian from statements received from the funds, partnerships or investment managers.

The pricing sources used by the master custodian provide daily prices for equity securities; corporate, government and mortgage-backed fixed income securities; private placement securities; futures and options on futures; open-ended funds; and foreign exchange rates. Depending on the vendor, collateralized mortgage obligations (CMOs), adjustable rate mortgages (ARMs) and asset-backed securities are priced either daily, weekly or twice a month and at month end. Municipal fixed income securities and options on U.S. Treasury/GNMA securities are priced at month end.

2. Investment Transactions and Income

Security transactions and related gains and losses are recorded on a trade date basis. The cost of investments sold is the average cost of the aggregate holding of the specific investment sold. Dividend income is recorded on the ex-dividend date, and interest income is accrued as earned. Futures contracts are valued daily, with the resulting adjustments recorded as realized gains or losses arising from the daily settlement of variation margin. Gains and losses related to forward contracts and options are recognized at the time the contracts are settled. Investments in limited partnerships are accounted for on the equity method of accounting, and their earnings or losses for the period are included in investment income using the equity method.

E. PROPERTY, PLANT, FURNITURE AND EQUIPMENT
Capital assets are recorded at cost at the time of acquisition and are reported net of accumulated depreciation. The System capitalizes all property, plant and equipment that have a cost or value greater than \$5,000. Depreciation is computed on the straight-line basis over the estimated useful life of the property, ranging from five to 40 years.

F. ACCUMULATED VACATION, SICK LEAVE AND DISABILITY CREDITS

Employees of the System participate in the Commonwealth's accumulated vacation program and in either its sick leave program or the Virginia Sickness and Disability Program (VSDP), which is administered by the System. Unused vacation may be accumulated and is paid at the time of permanent separation from service up to the maximum calendar year limit. Unused sick leave may be accumulated. If the member is vested, unused sick leave is paid at the rate of 25% of the amount accumulated, not to exceed \$5,000 at the time of permanent separation from service. Unused VSDP disability credits converted from unused sick leave are paid in the same manner as unused sick leave at the time of permanent separation. The accrued liability for unused vacation, sick leave or disability credits reflected in the accompanying statements at June 30, 2007 and 2006 was computed using salary rates in effect at those times and represents vacation and sick leave earned up to the allowable ceilings as well as unused, converted disability credits.

G. ADMINISTRATIVE EXPENSES AND BUDGET

The Board of Trustees approves expenses related to the administration and trust fund management activities of the System. These expenses are included in a budget prepared in compliance with the Commonwealth's biennial budgetary system (cash basis). Appropriations are controlled at the program level and lapse at the end of the fiscal year. Administrative expenses are funded exclusively from

investment income. Expenses for goods and services received but not paid for prior to the System’s fiscal year end are accrued for financial reporting purposes in accordance with generally accepted accounting principles (GAAP). A reconciliation of the difference between the GAAP basis and budgeted basis is presented in the Schedule of Administrative Expenses.

H. INVESTMENT INCOME ALLOCATION

Income earned on investments is distributed monthly to the Virginia Retirement System, the State Police Officers’ Retirement System, the Virginia Law Officers’ Retirement System, the Judicial Retirement System, the Group Life Insurance Fund, the Retiree Health Insurance Credit Fund and the Disability Insurance Trust Fund. Distribution of investment income is based on the respective equity of each trust fund in the common investment pool.

The retirement plans distribute their cumulative investment income, net of administrative expenses, in the following manner:

1. Investment income is distributed to each of the individual member accounts based on a rate of 4% applied to each member’s cumulative balance as of the close of the preceding fiscal year.
2. The remaining portion is allocated quarterly to the participating employer accounts based on the ratio of their member account and employer account balances to the total of all such balances.

2. Plan Description

A. RETIREMENT PLANS

The Virginia Retirement System was established on March 1, 1952 as the administrator of the Virginia Retirement System (VRS), a qualified governmental retirement plan that provides defined benefit coverage for state employees, public school board employees, employees of participating political subdivisions and other qualifying employees. VRS is a mixed agent and cost-sharing, multiple-employer retirement plan. The plan’s accumulated assets may legally be used to pay all plan benefits provided to any of the plan members or beneficiaries.

The System also administers single-employer retirement plans for state police officers, who are covered under a separate State Police Officers’ Retirement System (SPORS) established on July 1, 1950; state law enforcement and correctional officers other than state police officers, who are covered under the Virginia Law Officers’ Retirement System (VaLORS) established on October 1, 1999; and judges of a court of record or a district court of the state and other qualifying employees, who are covered under the Judicial Retirement System (JRS) established on July 1, 1970.

Distribution of VRS Employers at June 30, 2007 and 2006

	2007	2006
Cities and Towns	156	155
Counties	93	93
School Boards*	145	145
Special Authorities	183	181
State Agencies	<u>237</u>	<u>230</u>
Total Employers	<u>814</u>	<u>804</u>

* Of the 145 school boards, 132 also provide coverage for nonprofessional employees and are treated as political subdivisions by the System.

Membership Figures at June 30, 2007 and 2006

	2007				2007	2006
	VRS	SPORS	VaLORS	JRS	Total	Total
Retirees and Beneficiaries						
Receiving Benefits	127,487	991	1,618	404	130,500	124,639
Terminated Members Entitled to Benefits but Not Yet Receiving Them	32,063	66	354	9	32,492	30,854
Total	159,550	1,057	1,972	413	162,992	155,493
Active Plan Participants:						
Vested	212,557	1,418	5,981	366	220,322	216,684
Nonvested	114,288	467	4,080	58	118,893	116,232
Total	326,845	1,885	10,061	424	339,215	332,916

All full-time, salaried permanent employees of VRS-participating employers are automatically covered under VRS, SPORS, VaLORS or JRS with these exceptions: (1) certain full-time faculty and administrative staff of public colleges and universities; and (2) eligible classified employees of the two state teaching hospitals. These employees have the option to elect not to participate in the systems. Benefit provisions and all other requirements are established by Title 51.1 of the *Code of Virginia* (1950), as amended.

Benefits vest for all plans after five years of service. Members are eligible for an unreduced retirement benefit at age 65 if they have five years of service credit (age 60 for hazardous duty employees of participating political subdivisions) or at age 50 with at least 30 years of service credit if elected by the employer (age 50 with at least 25 years of service for hazardous duty employees of participating political subdivisions). Members may retire with a reduced benefit at age 50 if they have at least 10 years of service credit or at age 55 (age 50 for hazardous duty employees of participating political subdivisions) if they have at least five years of service credit.

Annual retirement benefits are payable monthly for life in an amount equal to 1.7% of eligible members' average final compensation (AFC) for each year of credited service. AFC is the average of the member's 36 consecutive months of highest creditable compensation. Benefits are actuarially reduced for members who retire prior to becoming eligible for unreduced retirement benefits. Members of SPORS and VaLORS as well as hazardous duty employees of participating political subdivisions may receive a monthly benefit supplement if they retire before age 65. Members of VaLORS hired before July 1, 2001 were allowed to make a one-time election to increase the multiplier from 1.7% to 2.0% instead of receiving the supplement. Members of VaLORS hired after June 30, 2001 have their benefit computed using the 2.0% multiplier and are not eligible for the supplement. Members of JRS receive weighted years of service credit for each year of actual service under JRS. VRS, SPORS, VaLORS and JRS also provide death and disability benefits. Cost-of-living increases, based on changes in the Consumer Price Index and limited to 5% per year, are granted in the second year of retirement and in every year thereafter.

As required by Title 51.1 of the *Code of Virginia* (1950), as amended, members contribute 5% of their annual compensation to the defined benefit plans. Employers may assume the 5% member contribution. If a member leaves covered employment, the accumulated contributions plus earned interest may be refunded to the member. Each participating employer is required by state statute to contribute the remaining amounts necessary to fund the retirement plans using the entry age normal actuarial cost method adopted by the Board of Trustees. State statute may be amended only by the General Assembly of Virginia.

B. GROUP AND OPTIONAL LIFE INSURANCE PROGRAMS

The Group Life Insurance Fund was established on July 1, 1960 for state employees, teachers and employees of political subdivisions participating in VRS; state police officers; other state law enforcement and correctional officers; judges; and other qualifying employees. The program provides life insurance for natural death coverage equal to a member's annual compensation rounded to the next highest \$1,000, and then doubled. Accidental death coverage is double the natural death coverage. The program also provides coverage for accidental dismemberment and accidental blindness as well as an accelerated death benefit for terminal conditions. Approximately 355,046 members were covered under the program at June 30, 2007.

Participating employers and their covered employees are required by Title 51.1 of the *Code of Virginia* (1950), as amended, to contribute to the cost of group life insurance benefits. Employers may assume the employees' contributions.

An Optional Group Life Insurance Fund was established on November 1, 1995 for members covered under the basic group life program as a

supplement to that plan. Members also may purchase optional life insurance on their spouses and/or dependent children. The optional program provides natural death coverage equal to one, two, three or four times the member's annual compensation rounded to the next highest \$1,000, up to a maximum of \$600,000. Spouse coverage is available up to one-half of the member's optional insurance amount. Minor children who are at least 15 days old can be insured for \$10,000, \$20,000 or \$30,000, depending on the option chosen by the employee. An additional accidental death and dismemberment benefit is payable for death or bodily injuries. Approximately 60,820 members were covered under this program at June 30, 2007.

Optional group life insurance coverage ends for members when they retire or terminate their employment, or when their basic coverage ends. Members who retire for disability may continue their optional coverage until age 65 provided they continue to pay the required insurance premiums. Spouse coverage terminates should a couple divorce or when the member leaves employment. Children's coverage ends with the termination of the member's coverage or when the child marries or turns 21 years of age (25 years of age for full-time college students).

Members who elect optional life insurance coverage are responsible for the premiums, which their employers deduct from their pay as required by Title 51.1 of the *Code of Virginia* (1950), as amended. Premium requirements are based on the member's age and determined by the Board of Trustees. Because optional life insurance is an insured product, the carrier bills each employer directly, and the employer makes the contribution payments to the carrier. Any differences and adjustments are settled between the employer and the carrier.

C. VIRGINIA SICKNESS AND DISABILITY PROGRAM

The Disability Insurance Trust Fund, also known as the Virginia Sickness and Disability Program (VSDP), was established on January 1, 1999 to provide benefits for full-time, classified state employees hired on or after January 1, 1999. Classified state employees include state police officers and other state law enforcement and correctional officers. Part-time permanent salaried state employees who work at least 20 hours a week and accrue leave also are covered. Eligible state employees and state police officers of the Commonwealth employed prior to January 1, 1999 had the option to elect to participate in the VSDP or remain under the Commonwealth's existing sick leave program and retain their eligibility for disability retirement benefits under VRS and SPORS. Eligible employees enrolled in VSDP are not eligible for disability retirement benefits under VRS, SPORS or VaLORS.

Teaching, administrative and research faculty of Virginia public institutions of higher education hired or appointed on or after January 1, 1999 who elected VRS as their retirement plan must make an irrevocable election to participate in the VSDP or in the institution's disability program. If there is no institution program, the faculty member is covered under VSDP.

By providing sick, family and personal leave and short-term and long-term disability benefits, the VSDP gives its members income protection from the first day of employment. After a seven-calendar day waiting period following the first incident of disability, eligible full-time and part-time classified employees receive short-term disability benefits from 60% to 100% of compensation, for a maximum of 125 work days, based on months of state service. After 125 work days of short-term disability, eligible employees receive long-term disability benefits equal to 60% of their

compensation until they return to work; until age 65 (age 60 for state police officers and other state law enforcement and correctional officers); or until death. Approximately 72,165 members were covered under the program at June 30, 2007.

State agencies are required by Title 51.1 of the *Code of Virginia* (1950), as amended, to contribute to the cost of providing long-term disability benefits and administering the program. Initial contribution requirements to fund the program were determined by the System's actuary using an estimate of the amount of liability for disability benefits that would transfer from VRS, SPORS and VaLORS to VSDP for the anticipated participants in VSDP.

3. Contributions – Retirement Plans

The funding policy of the retirement plans provides for periodic employer contributions at actuarially determined rates, which will remain relatively level over time as a percentage of payroll and will accumulate sufficient assets to meet the cost of all basic benefits when due. Contribution rates are developed using the entry age normal cost method for both normal cost and amortization of the unfunded actuarial accrued liability. Gains and losses are reflected in the unfunded actuarial accrued liability that is being amortized as a level percentage of payroll within 30 years or less.

The amount of contributions to be provided by employers for state employees, each participating political subdivision, the State Police Officers' Retirement System, the Virginia Law Officers' Retirement System and the Judicial Retirement System was actuarially computed by Wachovia Retirement Services. The contribution rates for FY 2007 were based on their valuation as of June 30, 2005. In addition, a separate contribution requirement was computed for the teacher cost-sharing pool by the actuary for each year using the same valuation date noted above. The

Contributions for the Years Ending June 30, 2007 and 2006

(EXPRESSED IN THOUSANDS)

	2007				2007	2006
	VRS	SPORS	VaLORS	JRS	Total	Total
Employer Contributions	\$ 1,124,535	\$ 16,358	\$ 48,322	\$ 20,530	\$ 1,209,745	\$ 865,894
Member Contributions						
Paid by Employer	680,023	4,895	16,127	2,815	703,860	661,014
Member Contributions	29,489	213	371	92	30,165	39,771
Total Contributions	\$ 1,834,047	\$ 21,466	\$ 64,820	\$ 23,437	\$ 1,943,770	\$ 1,566,679

contributions for FY 2006 were computed by Gabriel, Roeder, Smith & Company during their actuarial valuation as of June 30, 2003.

Contributions totaling \$1,943,770,000 and \$1,566,679,000 for the fiscal years ended June 30, 2007 and 2006, respectively, were made by employers and members in accordance with statutory requirements. These contributions covered employers' normal costs and amortization of unfunded actuarial accrued liabilities.

Total employer contributions were \$1,209,745,000 for FY 2007. Included in total employer contributions were \$431,000 from school boards for payments toward early retirement program costs and \$3,400,000 from state agencies for payments toward Workforce Transition Act (WTA) costs. Included in the member contributions of \$30,165,000 were \$28,010,000 paid for the purchase of previously refunded service and other qualifying service.

Employer contributions to the VRS cost-sharing pool for teachers represented 9.20% of covered payrolls. Additionally, the employer contributions to VRS by the state for state employees were 5.74% of covered payroll. Each political subdivision's contributions ranged from zero (0.00%) to 25.96% of covered payrolls. Employer contributions to SPORS by the state represented 16.71%; employer contributions to VaLORS by the state represented 14.96%; and employer

contributions to JRS by the state represented 36.47% of covered payrolls. This was an increase from the employer contribution rates used in FY 2006, which were 6.62% for teachers, 3.91% for state employees, 16.49% for employees in SPORS, 16.99% for employees in VaLORS and 30.55% for employees in JRS. For FY 2006, employer contributions for political subdivisions ranged from zero (0.00%) to 22.00%. Member contributions for both years represented 5.00% of covered payrolls. Employer and member contributions are required by Title 51.1 of the *Code of Virginia* (1950), as amended.

In addition to determining contribution requirements, the actuarial computations present an estimate of the discounted present value of the prospective accrued liability contributions that employers will have to pay in the future so that such contributions, together with the assets on hand, the normal contributions to be made in the future by employers and members and the income earned by investing the funds, will be sufficient to provide all benefits to be paid to present members in the future as well as to annuitants and their designated beneficiaries. Historical trend information regarding the System's progress in accumulating sufficient assets to pay benefits when due is presented in the Required Supplemental Schedule of Funding Progress – Pension Plans.

4. Other Post-Employment Benefits (OPEB)

The Government Accounting Standards Board (GASB) issued Statement No. 43, Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans, which requires additional reporting and disclosures for other post-employment benefit (OPEB) plans. The statement became effective for VRS-administered OPEB plans beginning with the fiscal year ended June 30, 2007. The assets and actuarial accrued liabilities for the following other post-employment benefits (OPEB) were determined through an actuarial valuation performed as of June 30, 2006 by Wachovia Retirement Services, and are presented in the Required Supplemental Schedule of Funding Progress – Other Post-Employment Benefits.

A. LIFE INSURANCE BENEFITS

Employees who retire or terminate from service after age 50 with at least 10 years of service or at age 55 with at least five years of service (age 50 for state police officers, other state law enforcement and correctional officers and hazardous duty employees of participating political subdivisions), or who retire because of disability, are entitled to post-employment life insurance benefits. At retirement or termination, accidental death benefits cease and natural death coverage reduces at a rate equal to 25% on January 1 of the first full year following retirement or termination and each year thereafter, until it reaches 25% of its original value. These group life insurance benefit provisions and requirements are established by Title 51.1 of the *Code of Virginia* (1950), as amended. There were approximately 122,947 retirees in the program in FY 2007.

Since 1960, when the group life insurance program was established, a portion of the premium contributions collected during

members' active careers has been placed in an Advance Premium Deposit Reserve. This reserve was established to pre-fund death benefits to members after retirement.

Employers providing life insurance benefits are part of a cost-sharing pool. Therefore, separate measurements of assets and actuarial accrued liabilities are not made for individual employers participating in the program.

B. RETIREE HEALTH INSURANCE CREDIT PROGRAM

The Retiree Health Insurance Credit Fund was established on January 1, 1990 and provides benefits for retired state employees, state police officers, other state law enforcement and correctional officers and judges who have at least 15 years of service credit under the retirement plans. The program provides a maximum credit reimbursement of \$4 per month per year of service credit against the monthly health insurance premiums of eligible retirees.

A similar program was established on July 1, 1993 to provide benefits for retired teachers and employees of participating political subdivisions with at least 15 years of service credit under the retirement plans. Retired teachers may receive a monthly credit ranging from \$75 to \$105, and local government retirees may receive a maximum credit of \$45.

Benefit provisions and eligibility requirements are established by Title 51.1, Chapter 14 of the *Code of Virginia* (1950), as amended. The amount required to fund all credits is financed on a current disbursement basis by the employers based on contribution rates determined by the System's actuary. Approximately 76,119 retired members were covered under this program at June 30, 2007.

C. VIRGINIA SICKNESS AND DISABILITY PROGRAM

The Commonwealth of Virginia provides OPEB disability insurance benefits, in accordance with state statutes, to eligible retired and terminated employees. There were approximately 2,178 former members receiving benefits from the program during FY 2007. Note 2C provides information regarding eligibility requirements and benefit provisions.

The Disability Insurance Trust Fund is funded by employer contributions and investment income. It is charged for long-term disability benefits and for expenses incurred in operating the Virginia Sickness and Disability Program.

5. Reserve Accounts

The reserve account balances available for benefits at June 30, 2007 and 2006 are presented in the table shown on this page. These funds are required by Titles 51.1 and 2.1 of the *Code of Virginia* (1950), as amended, to provide for the payment of current and future benefits.

Member and employer reserves are funded by member and employer contributions and investment income. Each member has an account that accumulates member contributions plus annual interest. Each employer has an account that accumulates employer contributions, transfers of investment income reduced by the administrative expenses incurred in operating the retirement plans and transfers of member contributions and interest upon a member's retirement. Employer accounts are charged with benefit payments.

The Advance Premium Deposit Reserve accumulates a portion of insurance premium contributions collected during a member's active career and their investment earnings, and is charged for death benefits paid and expenses incurred in operating the group life insurance program.

The Retiree Health Insurance Credit Reserve is funded by employer contributions and investment income. It is charged for credit reimbursements applied to the monthly health insurance premiums of eligible retired members and for expenses incurred in operating the Retiree Health Insurance Credit Fund program.

Reserve Balances Available for Benefits at June 30, 2007 and 2006

(EXPRESSED IN THOUSANDS)

	2007	2006
Virginia Retirement System		
Member Reserve	\$ 8,838,174	\$ 7,658,117
Employer Reserve	46,110,049	38,362,617
Total VRS	54,948,223	46,020,734
State Police Officers' Retirement System		
Member Reserve	70,778	67,037
Employer Reserve	613,171	513,334
Total SPORS	683,949	580,371
Virginia Law Officers' Retirement System		
Member Reserve	174,221	161,512
Employer Reserve	694,145	538,411
Total VaLORS	868,366	699,923
Judicial Retirement System		
Member Reserve	33,528	31,379
Employer Reserve	356,137	294,306
Total JRS	389,665	325,685
Group Life Insurance		
Advance Premium Deposit Reserve	962,328	751,361
Retiree Health Insurance Credit Reserve	224,606	178,068
Virginia Sickness and Disability Program		
Disability Insurance Trust Fund	263,586	191,872
Total Pension and Other Employee Benefit Reserve	\$ 58,340,723	\$ 48,748,014

6. Deposits and Investments

The Governmental Accounting Standards Board (GASB) Statement No. 40, Deposit and Investment Risk Disclosures, requires disclosures related to investment risk. Required investment risk disclosures address credit risk, including custodial credit risk and concentrations of credit risk, interest rate risk and foreign currency risk. The statement also requires disclosures of custodial credit risk and foreign currency risk for depository accounts.

Deposits at June 30, 2007 and 2006

(EXPRESSED IN THOUSANDS)

	2007 Carrying Amount	2006 Carrying Amount
Treasurer of Virginia	\$ 23,137	\$ 234,497
Master Custodian	<u>52,623</u>	<u>3,416</u>
Total Deposits	<u>\$ 75,760</u>	<u>\$ 237,913</u>

A. DEPOSITS

Deposits of the System maintained by the Treasurer of Virginia at June 30, 2007 and 2006 were entirely insured under the Virginia Security for Public Deposits Act, Section 2.2-4400 et seq. of the *Code of Virginia* (1950), as amended, which provides for an assessable multiple financial institution collateral pool. Deposits with the System's master custodian, Mellon Trust, were entirely insured by federal depository insurance coverage.

B. INVESTMENTS

1. Authorized Investments

The Board of Trustees of the System has full power to invest and reinvest the trust funds in accordance with Section 51.1-124.30 of the *Code of Virginia* (1950), as amended. This section requires the Board to discharge its duties solely in the interest of the beneficiaries and to invest the assets with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims. The Board also must diversify such instruments so as to minimize the risk of large losses unless, under the circumstances, it is clearly prudent not to do so.

Investment value and earnings of the investment pool are proportionally allocated among the System's trust funds on the basis of each fund's equity interest in the common investment pool. An Investment Summary is included in the Investment Section of this report. As of June 30, 2007 and 2006, the equity interests of each fund were as follows:

Equity Interests at June 30, 2007 and 2006

Fund	2007	2006
Virginia Retirement System	94.15%	94.35%
State Police Officers' Retirement System	1.17%	1.19%
Virginia Law Officers' Retirement System	1.49%	1.43%
Judicial Retirement System	0.67%	0.67%
Group Life Insurance Fund	1.69%	1.60%
Retiree Health Insurance Credit Fund	0.38%	0.36%
Disability Insurance Trust Fund	<u>0.45%</u>	<u>0.40%</u>
Total	<u>100.00%</u>	<u>100.00%</u>

Effective Duration of Debt Securities by Investment Type as of June 30, 2007

(EXPRESSED IN THOUSANDS)

Investment Type	Market Value June 30, 2007	Weighted Avg. Effective Duration (Years)
U.S. Government Agencies	\$ 2,431,379	5.00
Municipal Securities	4,593,342	4.46
Asset-Backed Securities	15,875	3.41
Collateralized Mortgage Obligations	1,303,005	0.48
Commercial Mortgages	707,050	1.25
Corporate Bonds and Other Bonds	395,737	4.27
Fixed-Income Commingled Funds	5,075,369	3.12
Cash and Cash Equivalents	1,248,250	3.97
	542,684	–
Total	<u>\$16,312,691</u>	3.37

2. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The risk is managed within the portfolio using the effective duration or option-adjusted methodology (see table above). It is widely used in the management of fixed income portfolios in that it quantifies, to a much greater degree, the risk of interest rate changes. The methodology takes into account optionality on bonds and scales the risk of price changes on bonds depending upon the degree of change in rates and the slope of the yield curve. All of the System's fixed income portfolios are managed in accordance with investment guidelines, most of which are specific as to the degree of interest rate risk that can be taken.

Credit Quality and Exposure Levels of Nongovernment Guaranteed Securities as of June 30, 2007

(EXPRESSED IN THOUSANDS)

Credit Rating Level	Agencies	Municipal Securities	Asset-Backed Securities	Collateralized Mortgage Obligations	Commercial Mortgages	Corporate and Other Bonds	Fixed-Income Commingled Funds	Cash and Cash Equivalents
U.S. Government								
Agencies	\$4,547,008	\$ -	\$ -	\$ 72,782	\$ -	\$ 6,730	\$ -	\$ -
AAA	-	-	-	-	-	-	-	147,817
Aaa	9,232	13,652	1,204,349	521,453	278,608	324,233	597,010	-
Aa1	-	-	22,335	1,788	609	162,419	-	-
Aa2	37,099	-	1,998	-	-	143,780	-	-
Aa3	-	-	6,993	-	-	449,384	-	-
A1	-	-	10,573	-	-	357,801	-	-
A2	-	-	14,244	-	-	376,270	-	-
A3	-	-	8,090	-	59	321,860	-	-
Baa1	-	-	1,382	887	-	393,758	213,573	-
Baa2	-	641	15,247	373	-	441,115	-	-
Baa3	-	-	2,934	-	-	349,844	-	-
Ba1	-	-	-	-	-	111,101	121,908	-
Ba2	-	-	-	-	-	58,837	-	-
Ba3	-	-	-	-	-	76,983	-	-
B1	-	-	-	-	-	84,743	-	-
B2	-	-	-	475	-	45,033	28,313	-
B3	-	-	-	-	-	54,745	267,016	-
Caa	-	-	-	-	-	-	20,430	-
Caa1	-	-	269	-	-	43,173	-	-
Caa2	-	-	-	-	-	19,470	-	-
Caa3	-	-	161	-	-	920	-	-
Ca	-	-	-	-	-	38	-	-
C	-	-	1,360	-	-	317	-	-
P-1	-	-	-	-	-	7,482	-	-
VMIG1	-	-	-	-	-	1,657	-	-
VMIG2	-	-	-	-	-	17,091	-	-
VMIG3	-	-	-	-	-	231	-	-
Not Rated	3	1,582	13,070	109,292	116,461	1,226,354	-	394,867
Total	\$4,593,342	\$ 15,875	\$1,303,005	\$ 707,050	\$ 395,737	\$ 5,075,369	\$1,248,250	\$ 542,684

3. Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to the System. As of June 30, 2007, the System's fixed income assets that are not government guaranteed represented 85% of the fixed income assets.

The System's policy for credit risk is based on the concept of a risk budget rather than specific limitations related to the rating of an individual security. The System's risk budget is allocated among the different investment strategies. The table on the previous page summarizes the System's fixed income portfolio exposure levels and credit qualities.

Credit risk for derivative instruments held by the System results from counterparty risk assumed by the System. This is essentially the risk that the borrower will be unable to meet its obligation. Information regarding the System's credit risk related to derivatives is found in the Derivative Financial Instruments note. Policies related to credit risk pertaining to the System's securities lending program are found in the Securities Lending note.

Concentration of Credit Risk

Concentration of credit risk is related to the risk of loss that may be attributed to the magnitude of a government's investment in a single issue. The System's investment guidelines for each specific portfolio limits investments in any corporate entity to no more than 5% of the market value of the account for both the internally and externally managed portfolios. There is no concentration of investments in any one organization that represents 5% or more of plan net assets available for benefits.

Custodial Credit Risk

Custodial credit risk is the risk that, in the event of the failure of the counterparty, the System will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. The System's market value of securities that were uninsured and held by a counterparty at June 30, 2007 and 2006 consisted of the following:

Custodial Credit Risk at June 30, 2007 and 2006

	(EXPRESSED IN THOUSANDS)	
	2007	2006
U.S. Government and Agency Mortgage Securities	\$138,245	\$194,798
Corporate and Other Bonds	3,552	–
Common and Preferred Stocks	–	48,409
Held by Broker-Dealers Under Securities Lending Program:		
U.S. Government and Agency Mortgage Securities	356,075	202,390
Common and Preferred Stocks	130,328	60,609
Total	\$628,200	\$506,206

4. Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. The System's currency risk exposures, or exchange rate risk, primarily exists in the international and global equity investment holdings. From time to time, the System's external

managers may hedge their portfolios' foreign currency exposures with currency forward contracts. This will depend on their views about a specific foreign currency relative to the U.S. dollar. The System's exposure to foreign currency risk is highlighted in the following table:

Currency Exposures by Asset Class as of June 30, 2007

(EXPRESSED IN THOUSANDS)

Currency	Cash and Cash Equivalents	Equity	Corporate Bonds	Private Equity	Real Estate	International Funds	Total
U.S. Dollar	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 4,865,259	\$ 4,865,259
Euro Currency Unit	12,682	1,686,524	11,281	648,439	30,379	-	2,389,305
British Pound Sterling	-	1,434,282	(13,092)	34,657	1,355	-	1,457,202
Australian Dollar	6,438	1,013,411	-	-	35,054	-	1,054,903
Canadian Dollar	1,738	602,488	(998)	-	6,868	-	610,096
Norwegian Krone	245	473,492	6,097	-	-	-	479,834
Hong Kong Dollar	3,239	353,445	-	-	31,975	-	388,659
New Taiwan Dollar	8,810	363,592	-	-	-	-	372,402
Swedish Krona	728	313,299	-	28,612	2,233	-	344,872
Japanese Yen	38,376	204,040	33,869	-	1,614	-	277,899
South Korean Won	839	239,372	-	-	-	-	240,211
Brazil Real	800	231,236	6,528	-	-	-	238,564
Indian Rupee	5,233	191,530	-	-	-	-	196,763
Mexican New Peso	313	127,887	-	-	-	-	128,200
South African Comm Rand	850	104,144	-	-	-	-	104,994
Singapore Dollar	237	75,984	-	-	16,798	-	93,019
New Turkish Lira	649	74,928	-	-	-	-	75,577
Thailand Baht	57	60,047	-	-	-	-	60,104
Israeli Shekel	930	57,303	-	-	-	-	58,233
Polish Zloty	283	40,158	-	-	-	-	40,441
Malaysian Ringgit	919	37,449	-	-	-	-	38,368
Danish Krone	264	33,319	-	-	-	-	33,583
Russian Ruble (New)	3	32,290	-	-	-	-	32,293
Egyptian Pound	451	26,592	-	-	-	-	27,043
Chinese Yuan Renminbi	-	24,242	-	-	-	-	24,242
Indonesian Rupian	116	14,824	-	-	-	-	14,940
Chilean Peso	-	12,714	-	-	-	-	12,714
Hungarian Forint	1,125	8,014	-	-	-	-	9,139
Turkish Lira	7,189	-	-	-	-	-	7,189
Romanian Leu	-	7,171	-	-	-	-	7,171
Pakistan Rupee	-	5,220	-	-	-	-	5,220
Philippines Peso	179	3,538	-	-	-	-	3,717
Argentina Peso	-	(10,561)	-	-	-	-	(10,561)
Czech Koruna	116	(20,868)	-	-	-	-	(20,752)
New Zealand Dollar	9	(171,285)	-	-	-	-	(171,276)
Swiss Franc	3,300	(496,776)	-	-	539	-	(492,937)
Total	\$ 96,118	\$ 7,153,045	\$ 43,685	\$ 711,708	\$ 126,815	\$ 4,865,259	\$12,996,630

5. Securities Lending

Under authorization of the Board, the System lends its fixed income and equity securities to various broker-dealers on a temporary basis. This program is administered through an agreement with the System's custodial agent bank. All security loan agreements are collateralized by cash, securities or an irrevocable letter-of-credit issued by a major bank, and have a market value equal to at least 102% of the market value for domestic securities and 105% for international securities. Securities received as collateral cannot be pledged or sold by the System unless the borrower defaults. Contracts require the lending agents to indemnify the System if the borrowers fail to return the securities lent and related distributions, and if the collateral is inadequate to replace the securities lent. All securities loans can be terminated on demand by either the System or the borrowers. The majority of loans are open loans, meaning the rebate is set daily. This results in a maturity of one or two days on average, although securities are often on loan for longer periods. The maturity of loans generally does not match the maturity of collateral investments, which averages 148 days. At year end, the System has no credit risk exposure to borrowers because the amounts it owes the borrowers exceed the amounts the borrowers owe it. The market value of securities on loan at June 30, 2007 and 2006 was \$6,329,913,000 and \$4,335,714,000, respectively. The June 30, 2007 and 2006 balances were composed of U.S. government and agency securities of \$2,604,362,000 and \$2,366,847,000, respectively; corporate and other bonds of \$409,177,000 and \$225,695,000, respectively; and common and preferred stocks of \$3,316,374,000 and \$1,743,172,000, respectively.

The value of collateral (cash and non-cash) at June 30, 2007 and 2006 was \$6,530,930,000 and \$4,421,712,000, respectively. Securities on loan are included with investments on the statement of net assets. The invested cash collateral is included in the statement of net assets as an asset and corresponding liability.

6. Accounts Receivable/Accounts Payable for Security Transactions

In addition to unsettled purchases and sales, accounts receivable and accounts payable for security transactions at June 30, 2007 and 2006, respectively, include (1) receivables for deposits with brokers for securities sold short of \$1,969,530,000 and \$1,142,069,000; and (2) payables for securities sold short and not covered with market values of \$1,960,937,000 and \$1,152,007,000, respectively.

7. Derivative Financial Instruments

Derivative instruments are financial contracts whose values depend on the values of one or more underlying assets, reference rates or financial indexes. They include futures, forwards, options and swap contracts. Some traditional securities, such as structured notes, can have derivative-like characteristics. In this case, the return may be linked to one or more indexes and asset-backed securities such as collateralized mortgage obligations (CMOs), which are sensitive to changes in interest rates and prepayments. Futures, forwards, options and swaps generally are not recorded on the financial statements, whereas structured notes and asset-backed investments generally are recorded.

The System is a party, both directly and indirectly, to various derivative financial investments that may or may not appear on the financial statements and that are used in the normal course of business to enhance returns on investments and manage risk exposure to changes in value resulting from fluctuations in market conditions. These investments may involve, to varying degrees, elements of credit and market risk in excess of amounts recognized on the financial statements. Credit risk is the possibility that loss may occur from the failure of a counterparty to perform according to the terms of the contract. Market risk arises from adverse changes in market prices, interest rates and foreign exchange rates that may result in a decrease in the market value of a financial investment or an increase in its funding cost, or both.

In addition to risk exposure from directly held derivative financial instruments, the System may have indirect exposure to risk through its ownership interests in commingled investment funds that use, hold or write derivative financial instruments. Indirect exposure also may arise from stock lending programs in which the commingled funds participate. Such programs usually reinvest a portion of their cash collateral holdings in derivative instruments. The System's pro rata share of the contractual or notional amounts of outstanding derivative transactions in commingled investment funds and their related security lending programs approximated \$98,034,000 at June 30, 2007 and \$237,369,000 at June 30, 2006.

8. Forward, Futures and Option Contracts

Forward contracts are contracts to purchase or sell; futures contracts are contracts to deliver or receive financial instruments, foreign currencies or commodities at a specified future date and at a specified price or yield. Futures contracts are

traded on organized exchanges (exchange-traded) and require initial margin (collateral) in the form of cash or marketable securities. The net change in the futures contract value is settled daily, in cash, with the exchanges. Holders of futures contracts look to the exchange for performance under the contract and not to the entity holding the offsetting futures position. Accordingly, the amount at risk posed by nonperformance of counterparties to futures contracts is minimal. In contrast, forward contracts traded over-the-counter are generally negotiated between two counterparties. They are subject to credit risks resulting from nonperformance of one of the counterparties and to market risks resulting from adverse fluctuations in market prices, interest rates and foreign exchange rates.

Options may be either exchange-traded or negotiated directly between two counterparties over-the-counter. Options grant the holder the right, but not the obligation, to purchase or sell a financial instrument at a specified price and within a specified period of time from the "writer" of the option. As a purchaser of options, the System typically pays a premium at the outset. This premium is reflected as an asset on the financial statements. The System then retains the right but not the obligation to exercise the option and purchase the underlying financial instrument. Should the option not be exercised, it expires worthless and the premium is recorded as a loss. A writer of options assumes the obligation to deliver or receive the underlying financial instrument on exercise of the option. Certain option contracts may involve cash settlements based on specified indexes such as stock indexes. As a writer of options, the System receives a premium at the outset. This premium is reflected as a liability on the financial statements and bears the risk of an unfavorable change in the price of the financial instrument underlying the option.

Forward, futures and options contracts provide the System with the opportunity to build passive benchmark positions; manage portfolio duration in relation to various benchmarks; adjust portfolio yield curve exposure; and gain market exposure to various indexes in a more efficient way and at lower transaction costs. Credit risks depend on whether the contracts are exchange-traded or exercised over-the-counter. Market risks arise from adverse changes in market prices, interest rates and foreign exchange rates. At June 30, 2007, the System had purchased S&P, Russell Index, Treasury bonds and notes and global indices futures and options with a notional value of \$7,564,225,000, and sold Treasury bonds and notes and global indices futures and options with a notional value of \$678,124,000. At June 30, 2006, the notional values of the balances purchased and sold were \$5,462,482,000 and \$638,208,000, respectively. At June 30, 2007, the System had pledged as collateral U.S. Treasury and U.S. Government Agency securities with a total market value of \$1,018,385,000 as the margin requirement for futures contracts. At June 30, 2006, the market value of the pledged securities was \$158,220,000.

9. Foreign Exchange Contracts

Foreign exchange contracts include forward, futures and options contracts. They involve either the exchange of specific amounts of two currencies or the delivery of a fixed amount of a currency at a future date and specified exchange rate. Forward and futures contracts settle three or more business days from the contract date. Forward contracts are negotiated over-the-counter between two counterparties, while futures contracts are exchange-traded. Foreign currency options, which are either negotiated between two counterparties or exchanged-traded, grant the buyer the right, but not the obligation, to purchase or sell at a specified price a stated amount of an underlying currency at a future date. At June 30, 2007, the System had sold foreign currency

contracts with a notional value of \$9,498,313,000 and had purchased foreign currency contracts with a notional value of \$9,460,292,000. At June 30, 2006, the notional values of the foreign currency contracts sold and purchased were \$7,157,688,000 and \$7,160,565,000, respectively.

Foreign exchange contracts are used by the System to effect settlements and to protect the base currency (\$US) value of portfolio assets denominated in foreign currencies against fluctuations in the exchange rates of those currencies. The credit risk of currency contracts that are exchange-traded lies with the clearinghouse of the exchange where the contracts are traded. The credit risk of currency contracts traded over-the-counter lies with the counterparty, and exposure is usually equal to the unrealized profit on in-the-money contracts. The market risk in foreign currency contracts is related to adverse movements in currency exchange rates.

10. Swap Agreements

Swaps are negotiated contracts between two counterparties for the exchange of payments at certain intervals over a predetermined timeframe. The payments are based on a notional principal amount and calculated using either fixed or floating interest rates or total returns from certain instruments or indices. During FY 2007, the System entered into interest rate and total return swaps with a total notional value of \$1,772,046,000. For FY 2006, the total notional value was \$1,226,074,000. Swaps are used to manage risk and enhance returns. To reduce the risk of counterparty nonperformance, the System generally requires collateral on any material gains from these transactions.

7. Property, Plant, Furniture and Equipment for the Year Ending June 30, 2007

(EXPRESSED IN THOUSANDS)

	Balance June 30, 2006	Increases	Decreases	Balance June 30, 2007
Nondepreciable Capital Assets: Land	\$ 1,368	\$ -	\$ -	\$ 1,368
Total Nondepreciable Capital Assets	1,368	-	-	1,368
Depreciable Capital Assets:				
Building	4,632	-	-	4,632
Furniture and Equipment	5,335	111	-	5,446
Total Depreciable Capital Assets	9,967	111	-	10,078
Less Accumulated Depreciation:				
Building	926	115	-	1,041
Furniture and Equipment	3,629	342	-	3,971
Total Accumulated Depreciation	4,555	457	-	5,012
Total Depreciable Capital Assets – Net	5,412	(346)	-	5,066
Total Capital Assets – Net	\$ 6,780	\$ (346)	\$ -	\$ 6,434

Depreciation expense amounted to \$457,000 and \$370,000 in 2007 and 2006, respectively.

8. Operating Leases

The System has commitments under various operating leases for equipment and office space for some staff. In general, the leases are for a three-year term. In most cases, the System expects that in the normal course of business, these leases will be replaced by similar leases. Total rental expense for the year ended June 30, 2007 was \$1,904,000. The System has, as of June 30, 2007, the following total future minimum rental payments due under the above leases:

(EXPRESSED IN THOUSANDS)

Year	Amount
2008	\$ 1,373
2009	996
2010	813
2011	720
2012	738
2013-2018	3,690
Total Future Minimum Rental Payments	\$ 8,330

9. Defined Benefit Pension Plan

A. CONTRIBUTIONS TO PENSION PLAN

All full-time, salaried permanent employees of the System are employees of the Commonwealth and are included in the Commonwealth's participation in the Virginia Retirement System (VRS), a defined benefit pension plan administered by the System. The Commonwealth, not the System, has overall responsibility for contributions to this plan and other employee benefit plans.

B. OTHER INFORMATION

Note 2A provides information regarding types of employees covered, benefit provisions, employee eligibility requirements (including eligibility requirements for vesting) and the authority under which benefit provisions and employer/member obligations to contribute are established. Additional information on funding policy and contributions required and made can be found in Note 3. Information on the actuarial method and assumptions can be found in the Notes to Required Supplemental Schedules – Pension Plans.

Historical trend information showing the Commonwealth of Virginia's progress in accumulating sufficient assets to pay benefits when due is presented in the Commonwealth's Comprehensive Annual Financial Report for the fiscal year ended June 30, 2007.

10. Other Employee Benefit Programs

A. LIFE INSURANCE BENEFITS

The Commonwealth of Virginia participates in the System-administered group life insurance program, which provides post-employment life insurance benefits, in accordance with state statutes, to eligible retired and terminated employees. There were approximately 101,874 state employees and 48,422 state retirees in the program during FY 2007. Note 2B provides information regarding eligibility requirements and benefit provisions as well as contribution requirements for active members, and Note 4A provides information for retired and terminated members.

The System's contribution requirement for its employees for the fiscal year ended June 30, 2007 was 1.13% of covered payroll. For FY 2006, the contribution rate was zero. The System's contribution requirements for its employees for the fiscal years ended June 30, 2007 and 2006 were \$178,000 and zero, respectively. In April 2002, the General Assembly suspended contributions for the group life insurance program through June 30, 2004. This was subsequently extended by the General Assembly through June 30, 2006.

B. RETIREE HEALTH INSURANCE CREDITS

The Commonwealth of Virginia provides health insurance credit reimbursements, in accordance with state statutes, against the monthly health insurance premiums of its retirees who have at least 15 years of service credit. The monthly credit is \$4 per year of

service credit. There is no limit on the amount of the monthly credit for state employees. Approximately 31,876 state retirees were receiving health insurance credits at June 30, 2007. Note 4B contains information regarding eligibility requirements, benefit provisions and contribution requirements.

For the fiscal year ended June 30, 2007, state agencies were required to contribute to the program at the statutory rate of 1.07% of covered payroll. This is an increase from the rate of 1.04% established for FY 2006. The System's contribution requirements for its employees for the fiscal years ended June 30, 2007 and 2006 were \$165,000 and \$143,000, respectively.

C. VIRGINIA SICKNESS AND DISABILITY PROGRAM

By providing sick, family and personal leave and short-term and long-term disability benefits, the VSDP gives its members income protection from the first day of employment. At June 30, 2007, approximately 72,165 members were enrolled in the program.

For the fiscal year ended June 30, 2007, state agencies were required to contribute to the program at the statutory rate of 1.78% of payroll for state employees, state police officers and other state law enforcement and correctional officers. This was an increase from the rate of 1.65% established for FY 2006. The System's contribution requirements for its employees for the fiscal years ended June 30, 2007 and 2006 were \$276,000 and \$228,000, respectively. Note 2C provides information regarding eligibility requirements and benefit provisions for active members, and Note 4C provides information for retired and terminated members.

11. Litigation

The System, its Board of Trustees, officers and employees are defendants in claims and lawsuits that are either pending, in progress or have been settled since June 30, 2007. It is not reasonably possible at the present time to estimate the ultimate outcome of the System's liability, if any, with respect to the various proceedings. However, on the basis of advice received from the Attorney General and outside counsel who have reviewed the status of these claims and lawsuits, it is the opinion of management that such liability, if any, would not have a material adverse effect on the System's financial condition.

12. Risk Management

To cover its exposure to various risks of loss, the System, as an independent agency of the Commonwealth of Virginia, participates in the Commonwealth's self-insurance programs for state employee health care and risk management. The latter program includes property, general (tort) liability, medical malpractice and automobile plans. The System's employees are covered by the Commonwealth's Workers' Compensation program administered by the Department of Human Resource Management. In addition, the System is self-insured for fiduciary liability and director's and officer's liability under a program administered by the Commonwealth's Division of Risk Management. There were no claims in excess of coverage and no reductions in coverage during FY 2007 and the three preceding fiscal years.

13. Commitments

The System extends investment commitments in the normal course of business. At June 30, 2007 and 2006, these commitments amounted to \$4,268,619,000 and \$4,842,000,000, respectively.

14. Statutory Contribution Adjustment

For FY 2006, contributions were based on the June 30, 2003 actuarial evaluation, which used a 23-year funding period for the Unfunded Accrued Actuarial Liability (UAAL). The General Assembly revised the VRS actuary's data by extending the funding period for these groups from 23 years to 30 years. As a result, the rate for teachers was reduced from 8.10% to 7.82%, and the General Assembly funded 6.62% (the "normal cost" plus a portion of the shortfall) in FY 2006. The rate for state employees in the VRS plan was increased from 3.89% to 3.91%. For FY 2006, the rates for SPORS, VaLORS and JRS were 16.49%, 16.99% and 30.55%, respectively, or the rates recommended by the actuary based on the 30-year funding period.

For FY 2007, contributions were based on the June 30, 2005 actuarial evaluation, which used a 21-year funding period for the UAAL. The General Assembly revised the VRS actuary's data from the June 30, 2005 actuarial valuation by again extending the funding period for these groups from 21 years to 30 years. As a result, the rate for teachers was reduced from 11.18% to 9.20%, and the rate for state employees was reduced from 7.33% to 5.74%. Additionally, the rates for SPORS, VaLORS and JRS were reduced from the actuary's recommended rates of 19.82%, 17.39% and 40.07% to 16.71%, 14.96% and 36.47%, respectively.

Required Supplemental Schedule of Funding Progress – Pension Plans

(DOLLARS IN MILLIONS)

Actuarial Valuation Date June 30	Actuarial Value of Assets (a)	Actuarial Liability (AAL) - Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll (b-a)/(c)
VIRGINIA RETIREMENT SYSTEM (VRS)						
2006	\$ 42,669	\$ 52,822	\$ 10,153	80.8%	\$ 13,002	78.1%
2005 **	40,372	49,628	9,256	81.3%	12,212	75.8%
2004	39,691	43,958	4,267	90.3%	11,510	37.1%
2003	39,243	40,698	1,455	96.4%	10,885	13.4%
2002	38,957	38,265	(692)	101.8%	10,669	(6.5%)
2001	37,968	35,384	(2,584)	107.3%	10,145	(25.5%)
2000 **	34,392	32,643	(1,749)	105.4%	9,529	(18.4%)
1999	29,804	31,419	1,615	94.9%	9,138	17.7%
1998 *	25,481	29,027	3,546	87.8%	8,638	41.1%
1996 **	19,032	23,842	4,810	79.8%	7,769	61.9%
STATE POLICE OFFICERS' RETIREMENT SYSTEM (SPORS)						
2006	\$ 539	\$ 730	\$ 191	73.8%	\$ 94	204.1%
2005 **	514	673	159	76.4%	91	174.8%
2004	510	656	146	77.8%	82	178.0%
2003	509	616	107	82.6%	79	135.4%
2002	508	595	87	85.4%	81	107.4%
2001	495	557	62	88.9%	83	74.7%
2000 **	441	513	72	86.0%	81	88.9%
1999	377	463	86	81.4%	77	111.7%
1998 *	322	425	103	75.8%	65	158.5%
1996 **	243	371	128	65.5%	60	213.3%
VIRGINIA LAW OFFICERS' RETIREMENT SYSTEM (VaLORS)						
2006	\$ 656	\$ 1,096	\$ 440	59.9%	\$ 321	137.0%
2005 **	575	980	405	58.7%	307	132.0%
2004	509	927	418	54.9%	298	140.3%
2003	458	854	396	53.6%	292	135.6%
2002	418	806	388	51.9%	306	126.8%
2001	393	628	235	62.6%	320	73.4%
2000 ***	307	680	373	45.1%	315	118.4%
JUDICIAL RETIREMENT SYSTEM (JRS)						
2006	\$ 302	\$ 424	\$ 122	71.3%	\$ 54	224.1%
2005 **	288	402	114	71.5%	52	220.7%
2004	285	366	81	78.0%	48	168.8%
2003	282	348	66	81.1%	48	137.5%
2002	281	352	71	79.8%	48	147.9%
2001	277	342	65	80.9%	47	138.3%
2000 **	245	330	85	74.2%	45	188.9%
1999	210	302	92	69.5%	42	219.0%
1998 *	180	274	94	65.7%	39	241.0%
1996 **	138	243	105	56.8%	36	291.7%

* Change in benefit formula, unreduced early retirement age and the actuarial amortization method.

** Revised economic and demographic assumptions due to experience study.

*** The first actuarial valuation for the Virginia Law Officers' Retirement System, established on October 1, 1999, was performed as of June 30, 2000.

Required Supplemental Schedule of Employer Contributions – Pension Plans

(DOLLARS IN THOUSANDS)

Year Ended June 30	Annual Required Contribution	Percentage Contributed	Statutory Required Contribution	Percentage Contributed
VIRGINIA RETIREMENT SYSTEM (VRS)				
2007 *	\$1,299,606	85.89%	\$1,116,217	100.00%
2006 *	864,245	89.51%	773,553	100.00%
2005 *	810,944	85.26%	691,415	100.00%
2004 *	469,200	91.66%	430,064	100.00%
2003 *	450,766	67.61%	304,784	100.00%
2002 *	459,613	79.68%	366,239	100.00%
2001 *	630,458	99.99%	630,370	100.00%
2000 *	785,376	93.24%	732,273	100.00%
1999 *	738,051	85.64%	632,084	100.00%
1998 *	757,164	71.06%	538,016	100.00%
STATE POLICE OFFICERS' RETIREMENT SYSTEM (SPORS)				
2007 *	\$ 19,402	84.31%	\$ 16,358	100.00%
2006 *	23,132	65.96%	15,258	100.00%
2005 *	21,946	65.96%	14,475	100.00%
2004 *	20,187	51.16%	10,328	100.00%
2003 *	19,866	44.20%	8,781	100.00%
2002 *	20,190	50.00%	10,095	100.00%
2001	20,420	100.00%	20,420	100.00%
2000 *	17,684	85.07%	15,044	100.00%
1999 *	16,088	69.87%	11,241	100.00%
1998 *	11,764	71.70%	8,435	100.00%
VIRGINIA LAW OFFICERS' RETIREMENT SYSTEM (VaLORS)				
2007 *	\$ 56,190	86.03%	\$ 48,338	100.00%
2006 *	77,414	67.96%	52,611	100.00%
2005 *	74,301	67.96%	50,495	100.00%
2004 *	72,752	55.80%	40,596	100.00%
2003 *	72,699	48.00%	34,895	100.00%
2002 *	77,417	32.30%	25,006	100.00%
2001	51,072	100.00%	51,072	100.00%
2000 **	16,216	84.81%	13,753	100.00%
JUDICIAL RETIREMENT SYSTEM (JRS)				
2007 *	\$ 22,557	91.02%	\$ 20,530	100.00%
2006 *	23,871	67.89%	16,206	100.00%
2005 *	22,490	67.89%	15,269	100.00%
2004 *	21,341	71.18%	15,190	100.00%
2003 *	21,110	64.44%	13,604	100.00%
2002 *	21,282	50.00%	10,641	100.00%
2001	20,822	100.00%	20,822	100.00%
2000 *	15,075	99.07%	14,935	100.00%
1999 *	14,118	91.64%	12,938	100.00%
1998 *	12,873	86.74%	11,166	100.00%

* Contributions made by employers during the fiscal years ended June 30, 1998, 1999, 2000, 2001, 2002, 2003, 2004, 2005, 2006 and 2007 were not in all cases in accordance with the actuarially determined Annual Required Contribution (ARC), but they did meet the statutory requirements. Beginning with FY 1998, all employers were provided an option to elect an annual contribution that met the parameters of the ARC, which includes full pre-funding of the automatic cost-of-living increases (COLAs) for retirees, or an annual contribution that would phase in the parameters over a five-year period ending with FY 2003.

** The VaLORS program went into effect on October 1, 1999.

Notes to Required Supplemental Schedules – Pension Plans – Actuarial Methods and Significant Assumptions

The information presented in the required supplementary 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	
State Employees	Level Percent, Closed
Teachers	Level Percent, Closed
Political Subdivision Employees	Level Percent, Closed
State Police/VA Law Officers/Judges	Level Percent, Closed
Payroll Growth Rate	
State Employees	3.00%
Teachers	3.00%
Political Subdivision Employees	2.50%
State Police/VA Law Officers/Judges	3.00%
Remaining Amortization Period	
State Employees	20 Years
Teachers	20 Years
Political Subdivision Employees	20 Years
State Police/VA Law Officers/Judges	20 Years
Asset Valuation Method	5-Year Smoothed Market
Actuarial Assumptions	
Investment Rate of Return *	7.50%
Projected Salary Increases *	
State Employees	3.75% to 5.60%
Teachers	3.75% to 6.20%
Political Subdivision	
Non-Hazardous Duty Employees	3.75% to 5.60%
Political Subdivision	
Hazardous Duty Employees	3.50% to 4.75%
State Police/VA Law Officers	3.50% to 4.75%
Judges	3.50%
Cost-of-Living Adjustments	2.50%

* Includes inflation at 2.50%.



Active members comprised 339,215 of
VRS' total membership of 582,469 at
June 30, 2007.

Required Supplemental Schedule of Funding Progress – Other Post-Employment Benefit Plans

(DOLLARS IN THOUSANDS)

Actuarial Valuation Date June 30	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)
GROUP LIFE INSURANCE FUND						
2006*	\$ 751,361	\$ 1,435,740	\$ 684,379	52.3%	\$13,922,762	4.9%
RETIREE HEALTH INSURANCE CREDIT FUND						
2006*	\$ 175,223	\$ 1,315,961	\$ 1,140,738	13.3%	\$ 9,964,627	11.4%
DISABILITY INSURANCE TRUST FUND						
2006*	\$ 191,872	\$ 422,886	\$ 231,014	45.4%	\$ 3,715,897	6.2%

* 2006 was the first actuarial valuation prepared using the required parameters of GASB 43. There is no Schedule of Employer Contributions included in this report since the first contributions paid based on the valuation using the GASB 43 parameters did not occur until FY 2008. These results will be included in the FY 2008 CAFR and Schedule of Employer Contributions.

Notes to the Required Supplemental Schedule – Other Post-Employment Benefits – Actuarial Methods and Significant Assumptions

The information presented in the required supplementary schedule was determined as part of an actuarial valuation at the date indicated. Additional information as of the latest actuarial valuation follows:

	Group Life Insurance Fund	Retiree Health Insurance Credit Fund	Disability Insurance Trust Fund
Valuation Date	June 30, 2006	June 30, 2006	June 30, 2006
Actuarial Cost Method	Entry Age Normal	Entry Age Normal	Projected Unit Credit
Amortization Method	Level Percent, Open	Level Percent, Open	Level Percent, Open
Payroll Growth Rate:			
State Employees	3.00%	3.00%	3.00%
Teachers	3.00%	3.00%	3.00%
Political Subdivision Employees	2.50%	2.50%	2.50%
State Police/VA Law Officers/Judges	3.00%	3.00%	3.00%
Remaining Amortization Period	30 Years	30 Years	30 Years
Asset Valuation Method	5-Year, Smoothed Market	5-Year, Smoothed Market	Market Value
Actuarial Assumptions:			
Investment Rate of Return *	7.50%	7.50%	7.50%
Projected Salary Increases: *			
State Employees	3.75% to 5.60%	N/A	3.75% to 5.60%
Teachers	3.75% to 6.20%	N/A	3.75% to 6.20%
Political Subdivision Non-Hazardous Duty Employees	3.75% to 5.60%	N/A	3.75% to 5.60%
Political Subdivision Hazardous Duty Employees	3.50% to 4.75%	N/A	3.50% to 4.75%
State Police/VA Law Officers	3.50% to 4.75%	N/A	3.50% to 4.75%
Judges	3.50%	N/A	3.50%

*Includes inflation at 2.50%

Schedule of Administrative Expenses for the Years Ended June 30, 2007 and 2006

(EXPRESSED IN THOUSANDS)

	2007	2006
Personal Services		
Salaries and Wages	\$ 17,407	\$ 15,704
Per Diem Services	365	291
Retirement Contributions	1,734	1,302
Social Security	1,166	1,036
Group Life and Medical Insurance	2,484	1,936
Compensated Absences	386	280
Total Personal Services	23,542	20,549
Professional Services		
Data Processing	4,564	3,944
Actuarial and Consulting	916	1,008
Legal	565	727
Medical	141	154
Management Services	702	340
Personnel Development Services	131	79
Total Professional Services	7,019	6,252
Communication Services		
Media	33	25
Printing	959	734
Postal and Delivery	544	520
Telecommunications	554	489
Total Communication Services	2,090	1,768
Rentals		
Business Equipment	904	775
Office Space	1,000	791
Total Rentals	1,904	1,566
Other Services and Charges		
Skilled and Clerical Services	127	158
Depreciation	457	370
Dues and Memberships	124	91
Building Expense	285	269
Equipment	1,318	1,111
Insurance	28	32
Repairs and Maintenance	60	8
Supplies and Materials	138	176
Travel and Transportation	455	600
Miscellaneous	102	85
Total Other Services and Charges	3,094	2,900
Total Administrative Expenses (GAAP Basis)	37,649	33,035
Adjustments Necessary to Convert Administrative Expenses on the GAAP Basis to the Budgetary Basis at Year End (Net)	(1,411)	250
Administrative Expenses (Budgetary Basis)	\$ 36,238	\$ 33,285
Administrative Expenses Appropriated	\$ 43,018	\$ 35,466
Distribution of Administrative Expenses		
Total Administrative Expenses (GAAP Basis)	\$ 37,649	\$ 33,035
Less In-House Investment Management	(11,438)	(11,058)
Net Administrative Expenses	\$ 26,211	\$ 21,977

Schedule of Professional and Consulting Services for the Year Ended June 30, 2007

(EXPRESSED IN THOUSANDS)

Actuarial, Legal and Oversight Services			
Joint Legislative Audit Review Commission	Oversight Responsibilities	93.2	
Wachovia Securities	Actuarial Services & Benefits Consulting	409.1	
Troutman Sanders, LLP	Legal Services	57.8	
Williams Mullins	Legal Services	60.8	
Subtotal Actuarial, Legal and Oversight Services			\$ 620.9
Consulting Services			
Advantage 2000	Social Security Advocacy & Disability Tracking	190.1	
Baskervill	Space Planning	54.2	
Bon Secours Memorial Regional Medical Center	Disability Medical Reviews	73.3	
CGI AMS Inc.	Imaging Assessment	67.3	
Clear Management	Administration Compensation Study	19.7	
Computer Aid, Inc.	IT Contractor	62.1	
CorVel Corporation	Physician Referral for Disability Cases	67.0	
Cost Effectiveness Measurement, Inc.	Cost Driver Benchmarking Analysis	18.5	
Ennis Krupp & Associates, Inc.	Investment Compensation Study	55.8	
R. Lewis Harrison	Fact Finding Hearing Officer for Disability Cases	12.9	
Hewitt Associates	Retirement Benefits Planning Tool	44.2	
McLagan Partners, Inc.	Investment Compensation Study	18.7	
Medical Board	Medical Examiners	58.2	
Milliman, Inc	Long Term Care Plan Consulting	232.5	
North Highland	Business Continuity Plan Consulting	34.0	
Northrop Gruman	Risk Management/BPR Consulting	243.4	
Property & Portfolio Research, Inc.	Investment Consulting Services	76.2	
Social Security Disability Consultants	Social Security Advocacy & Disability Tracking	215.9	
Southeastern Institute of Research, Inc.	Customer Research and Surveys	77.8	
Strategic Economic Decisions, Inc.	Economic Advisory Services	10.0	
Townsend Group	Investment Consulting Services	192.5	
Vector Consultants	IT Contractor	37.5	
Subtotal Consulting Services			\$ 1,861.8
Total			\$ 2,482.7

Schedule of Investment Expenses for the Year Ended June 30, 2007

(EXPRESSED IN THOUSANDS)

Management Fees			
Domestic Managers	\$	28,651	
Non-U.S. Equity Managers		29,164	
Global Equity Managers		20,099	
Fixed Income Managers		7,528	
Credit Strategies Managers		15,876	
Real Estate Managers		19,849	
Alternative Investment Managers		72,007	
Hedge Fund Managers		33,290	
			\$ 226,464
Performance Fees			10,562
Total Management Fund Performance Fees			\$ 237,026
Miscellaneous Fees and Expenses			
Custodial Fees	\$	4,146	
Legal Fees		122	
Other Fees and Expenses		585	
			\$ 4,853
In-House Investment Management			11,438
Total Investment Expenses			\$ 253,317

Investment Section

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Fees and Expenses
Investment Summary



...the right information...

During FY 2007, VRS staff:

- Counseled more than 2,200 member visitors to VRS about their retirement benefits.
- Provided benefits and retirement education for more than 10,600 members who attended sessions, presentations and benefit fairs around the state.
- Interacted with about 1,500 employer contacts through training sessions, site visits, forums and workshops.
- Maintained and updated the VRS Web site, which attracted 995,907 visits, a 27.2% increase over the visits logged in FY 2006.
- Maintained and updated a communication program consisting of four member benefit handbooks and a retiree handbook as well as publishing newsletters for members, retirees and employers throughout the year. Staff also maintained and updated the VRS Employer Manual designed to help participating employers administer VRS benefits.

Chief Investment Officer's Letter



Charles W. Grant, CFA, Chief Investment Officer

P.O. Box 2500, 1200 East Main Street
Richmond, Virginia 23218-2500

Toll Free: 1-888-VARETIR (827-3847); TDD: (804) 344-3190

November 8, 2007

**To the Members of the Board of Trustees and
Participants of the Virginia Retirement System:**

I am pleased to report that the VRS investment fund returned 20.4% for the fiscal year ending June 30, 2007. All asset classes performed well, and the fund exceeded performance benchmarks established by the Board of Trustees.

U.S. economic growth slowed over the last year, primarily due to weakness in the housing sector. Offsetting slower domestic growth were a very strong international economy and stable interest rates. In this environment, corporate earnings were healthy, creating strong support for attractive returns across the asset classes.

Equity investments performed exceptionally well. The fund's public equity portfolio returned 24.5%, while private equity investments returned 32.0%. VRS continued to benefit from a longstanding policy of maintaining a significant equity exposure. At year-end, equity investments represented approximately 71% of the fund.

Commercial real estate investments also were strong, providing a 23.8% return. Operating fundamentals were healthy, and the asset class benefited from strong investor demand. Real estate investments represented approximately 5% of the fund at year-end.

Credit and fixed income investments returned 13.6% and 6.0%, respectively. In total, credit and fixed income investments represented approximately 23% of the fund at year-end.

We recognize that fiscal 2007 was an unusually good year and not likely to be repeated very often. The portfolio is diversified in order to manage risk, and it is unusual for all asset classes to perform at such a high level at the same time. Our expectation is that returns will be more moderate over time and ultimately reflect the growth and earnings potential of the economy. The fund should be able to deliver returns of 7% to 8% over the long term.

Market volatility has been low in recent years due to the confluence of several positive factors. Inevitably, conditions will change in both the real economy and the financial markets, and volatility will likely increase. Given the nature of our liabilities, VRS has a long investment horizon. This is a strength in that we can afford to take prudent amounts of risk, and we are able to withstand market volatility in the pursuit of attractive long-term investments.

The global economy, capital markets and institutional investment strategies are all changing rapidly, creating a challenging environment for managing the fund. I appreciate the hard work of our talented investment team, a group that is committed to delivering good investment results for VRS. I would also like to thank the Investment Advisory Committee for their guidance and support.

The Board of Trustees has established an excellent policy and decision-making framework for managing VRS investments. The investment staff is appreciative of the Board's trust and support as we continue to manage risk and seek out attractive returns for the fund.

Respectfully submitted,

A handwritten signature in black ink that reads 'C. Grant'.

Charles W. Grant, CFA

Chief Investment Officer

Investment Account

The VRS Board of Trustees has fiduciary responsibility to invest the fund solely in the interest of the beneficiaries of the System. As established by the *Code of Virginia*, “the Board shall invest the assets of the Retirement System with the care, skill, prudence, and due diligence that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with like aims.”

Benefit payments are projected to occur over a long period of time. This allows VRS to adopt a long-term investment horizon and asset allocation policy for the management of fund assets. Asset allocation policy is critical because it defines the basic risk and return characteristics of the VRS investment portfolio. Asset allocation targets are established using an asset-liability analysis designed to assist the Board in determining an acceptable volatility target for the fund and an optimal asset allocation policy mix. This asset-liability analysis considers both sides of the VRS balance sheet in order to estimate the potential impact of various asset class mixes on key measures of total plan risk including the resulting estimated impact on funded status and contribution rates.

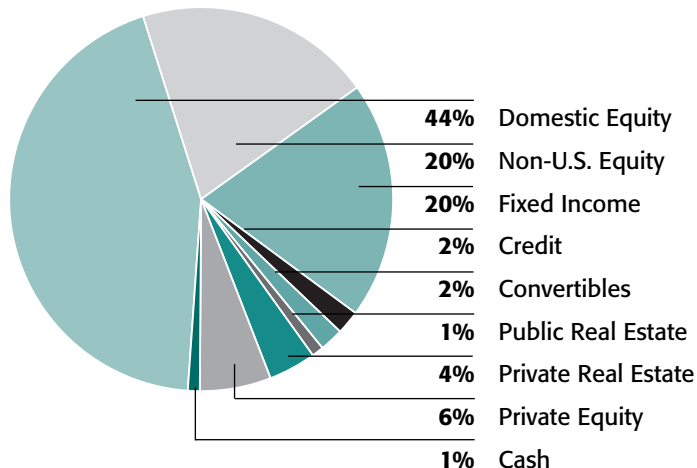
Benefit payments are projected to occur over a long period of time. This allows VRS to adopt a long-term investment horizon and asset allocation policy for the management of fund assets.

The Chief Investment Officer has been delegated authority by the Board to allocate the System’s investments within the approved asset allocation policy and within the Board approved active risk budget. The total fund active risk budget describes the degree of tolerance for yearly variation in the fund’s performance relative to the Intermediate Term Benchmark. The primary risk measure used for this purpose is Total Fund Tracking Error, calculated as the standard deviation of the difference between the fund’s return and the return of the Intermediate Term Benchmark. From this measure, probability estimates can be derived to help the Board estimate the risk of underperforming the benchmark by certain margins.

The investment staff manages the VRS portfolio on a day-to-day basis according to policies and guidelines established by the Board. The staff manages assets on a direct basis and through outside investment managers. Managers employ both active and passive investment strategies. The Board has established various performance benchmarks to serve as tools for measuring progress toward the achievement of intermediate and longer-term investment goals.

The asset allocation mix of the VRS fund as of June 30, 2007 is shown on the next page.

Asset Allocation Mix



Investment Performance Summary

ANNUALIZED DATA FOR PERIOD ENDING JUNE 30, 2007

	1 Year	3 Years	5 Years
1. Total Fund Time-Weighted Returns			
VRS	20.4%	14.9%	12.8%
Total Fund Intermediate Benchmark	18.5%	13.5%	12.0%
2. Total Public Equity			
VRS	24.5%	17.2%	14.8%
Custom Benchmark	23.4%	16.5%	14.4%
3. Total Fixed Income			
VRS	6.0%	4.1%	4.7%
Custom Benchmark	6.0%	4.0%	4.4%
4. Total Credit Strategies			
VRS	13.6%	8.8%	n/a
Custom Benchmark	13.5%	9.2%	n/a
5. Total Real Estate			
VRS	23.8%	23.8%	18.2%
Custom Benchmark	19.2%	20.5%	15.9%
6. Total Private Equity			
VRS	32.0%	27.3%	18.7%
Custom Benchmark	13.8%	13.3%	9.8%

Investment return calculations were prepared using a time-weighted return methodology.

Portfolio Highlights

Public Equity

The market value of the total Public Equity Program as of June 30, 2007 was \$37.6 billion, representing approximately 65% of the total fund. Roughly 68% was invested in Domestic Equity and 32% in International Equity. Thirteen percent of the Total Public Equity portfolio was invested in passive strategies, and 30% was managed internally. The objective of the portfolio is to exceed the return of the Custom Benchmark over three-year periods net of all costs. At year-end, the Custom Benchmark was comprised of 69% Russell 3000 and 31% of the S&P/Citigroup BMI Global (excluding U.S.).

The Total Public Equity Program outperformed the Custom Benchmark during the fiscal year by 1.1%. During the year, the Russell 3000 was up 20.1%, and the BMI Global (excluding U.S.) was up 30.8%. Emerging Markets and Non-U.S. small-capitalization indices

significantly outperformed U.S. indices. Solid earnings growth was the primary performance driver for nearly all markets as valuations remained reasonable.

The Total Public Equity Program is dominated (88.6% of program or \$33.3 billion) by traditional, long-only strategies. The program also employs traditional long-short strategies (4.8% of program or \$1.8 billion) and equity-oriented hedge fund strategies (6.6% of program or \$2.5 billion).

The Non-U.S. Equity Program utilizes a non-U.S. equity benchmark with un-hedged currency exposure. In an attempt to capitalize on currency market inefficiencies, staff utilizes risk-controlled active currency strategies that take long and short currency positions based on their fundamental attractiveness. The notional value of these strategies was \$5.0 billion as of June 30, 2007.

Total Public Equity Program Benchmarks

Benchmark Category	VRS Return *	Benchmark Return *	VRS Weight	Benchmark Weight
Russell 1000	20.5%	20.4%	34.2%	35.1%
Russell 2000	17.4%	16.4%	4.2%	3.3%
Russell 3000	22.4%	20.1%	12.0%	12.0%
Russell Special Small Cap	18.8%	18.9%	1.8%	1.9%
S&P 500	22.4%	20.6%	8.4%	8.2%
S&P/Citigroup PMI World	25.4%	23.9%	17.2%	17.2%
S&P/Citigroup PMI Emerging	39.4%	44.9%	4.9%	3.2%
S&P/Citigroup EMI World (ex US)	39.1%	31.7%	5.7%	4.3%
S&P/Citigroup PMI World (ex US)	27.5%	27.2%	11.6%	14.7%
Total Program	24.5%	23.4%	100.0%	100.0%

*One-Year Total Return June 30, 2007

Weights as of June 30, 2007

The VRS portfolio remained fairly close to the Custom Benchmark Sectors and Region weights.

Custom Benchmark Sectors and Regions

Sectors*	VRS	Strategic BM	Regions*	VRS	Strategic BM
Consumer Discretionary	11.7%	11.2%	North America	68.7%	70.7%
Consumer Staples	6.9%	7.7%	Europe/Australia/Far East	18.5%	17.9%
Energy	9.7%	9.9%	Asia/Pacific	10.9%	10.4%
Financials	22.4%	22.9%	Latin & South America	1.9%	1.0%
Health Care	9.3%	9.5%			
Industrials	12.0%	12.0%			
Information Technology	12.7%	12.9%			
Materials	6.8%	5.8%			
Telecommunication Services	5.0%	4.1%			
Utilities	3.5%	4.0%			

* Barra Sectors, Regions & Weights

The top 10 holdings in the total Public Equity Program comprised 9.4% of the program at year-end. In comparison to last year, one company fell from the list. Johnson & Johnson was replaced by AT&T Inc.

Public Equity: Top 10 Holdings

Company	Market Value	Shares
Exxon Mobil Corporation	\$ 579,607,602	6,909,962
General Electric Company	500,126,340	13,064,951
Microsoft Corporation	362,321,225	12,294,578
Citigroup Inc.	347,860,847	6,782,235
AT&T Inc.	337,576,075	8,134,363
Bank of America Corporation	314,558,382	6,434,002
Pfizer Inc.	279,910,187	10,946,820
Chevron Corp.	278,877,516	3,310,512
JP Morgan Chase & Co.	278,368,693	5,745,484
Altria Group Inc.	254,189,032	3,624,024

Fixed Income

VRS invests a portion of its portfolio in fixed income investments in order to reduce total fund volatility, produce income and provide for some protection in the event of a deflationary environment. At year-end, approximately \$11.2 billion was invested in fixed income assets, representing 20% of the VRS portfolio. Of this amount, approximately 50% was invested actively using outside managers, and 50% was invested in a more “risk-controlled” style (75% of this style is managed internally).

The objective of the entire program is to maximize the return (net of all costs) relative to the Citigroup Broad Investment Grade Index, while staying in compliance

with risk limits. The fixed income program return was 6.04% for the fiscal year.

The yield curve steepened over the last fiscal year as the market began to believe that the FOMC would lower interest rates by the end of calendar year 2007. As the housing market became more uncertain, and the sub prime mortgage story began to unfold, the bond market volatility (yield volatility) moved meaningfully higher. Spreads began to move in conjunction with the higher volatility, and by the end of the fiscal year, fears of a credit crunch were heightened. During the fiscal year, two-year rates decreased by 29 basis points to 4.86% and ten-year rates decreased by 11 basis points to 5.02%. Spreads were wider in all investment grade asset classes as investors migrated to the safety of U.S. treasury securities.

Fixed Income: Top 10 Holdings By Market Value

AS OF JUNE 30, 2007

Par	Security Description	Market Value
499,600,000	FNMA 5.50% 30-year MBS	\$ 481,756,570
265,090,000	FNMA 5.00% 30-Year MBS	248,280,970
176,200,000	FNMA 6.00% 30-Year MBS	174,233,671
123,420,000	U.S. Treasury Notes 4.500% due 4/30/2012	121,156,477
124,000,000	FHLMC 5.50% 30-year MBS	119,563,525
84,620,000	U.S. Treasury Notes 4.625% due 11/15/2009	84,116,511
64,400,000	GNMA 6.00% 30-Year MBS	64,058,680
56,200,000	FNMA 6.50% 30-Year MBS	56,728,280
54,975,000	U.S. Treasury Notes 4.625% due 11/15/2016	53,290,016
53,600,000	U.S. Treasury Notes 3.500% due 2/15/2010	51,783,496

Fixed Income Portfolio

AS OF JUNE 30, 2007

Sector Allocation	
Sector	% Portfolio
Treasury	17.0%
Agency	7.0%
Corporate	22.0%
Mortgage	41.0%
Asset Backed	1.0%
CMBS	4.0%
Foreign	0.0%
Other	8.0%
Total	100%

Credit Quality Breakdown	
Rating	% Portfolio
Government	27.6%
AAA	49.2%
AA	15.0%
A	2.3%
BBB	4.5%
BB	0.8%
B	0.2%
Below B	0.0%
NR	0.4%
Total	100%

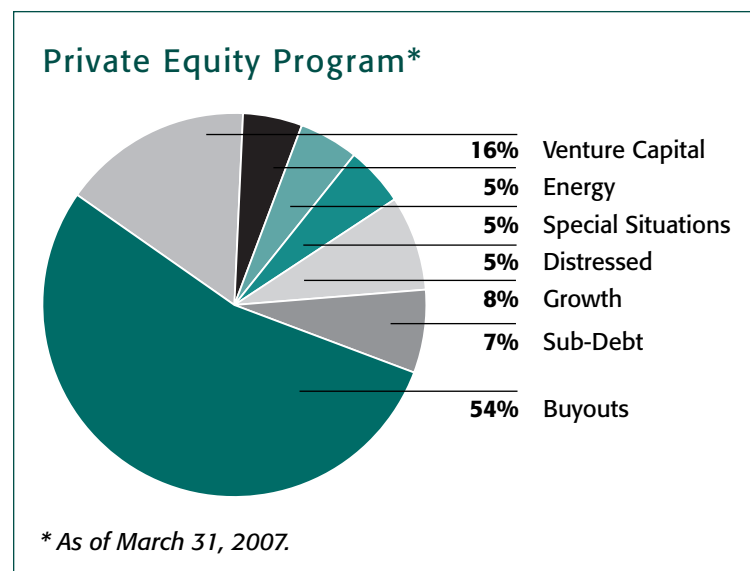
Short-Term Investments

As a rule, VRS desires to remain fully invested at all times and seeks to minimize its holdings of cash investments. Temporary cash balances are invested in short-term money market instruments with the goal of maintaining high credit quality and liquidity. The return on such investments approximates the return on the 30-day London Interbank Offered Rate (LIBOR), which averaged 5.36% over the last year.

Private Equity

VRS invests in private equity in order to achieve returns greater than those available in the public equity markets. Specifically, the program seeks to outperform the Russell 3000 Index by 2.5% per year. Program returns are calculated on both a time-weighted basis and a dollar-weighted or internal rate-of-return basis. On a time-weighted basis, the program return for FY 2007 was 32.0%. On a dollar weighted or internal rate of return (IRR) basis, the private equity program returned 33.1% (as of March 31, 2007). Both return metrics significantly outperformed the public equity market. This marks the fourth consecutive year the private equity program has generated a return exceeding 20%. The substantial returns over the last four years have been due primarily to a strong exit environment for buyout funds and improving fundamentals for venture capital funds.

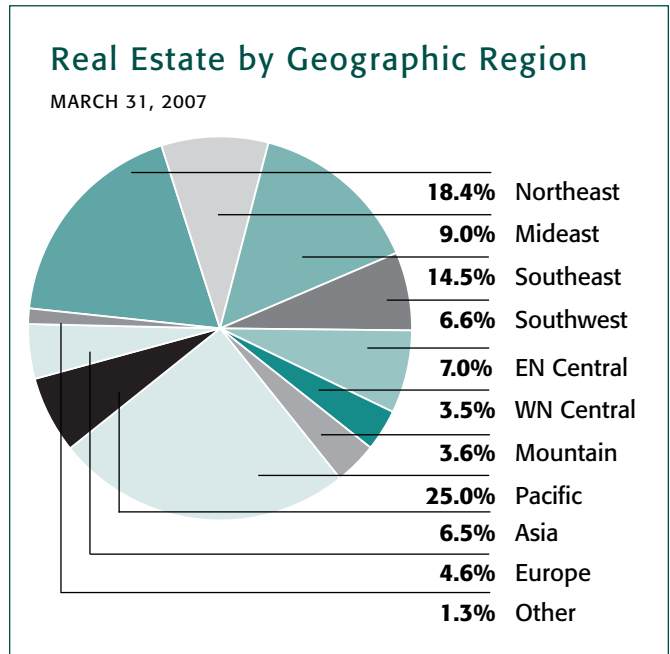
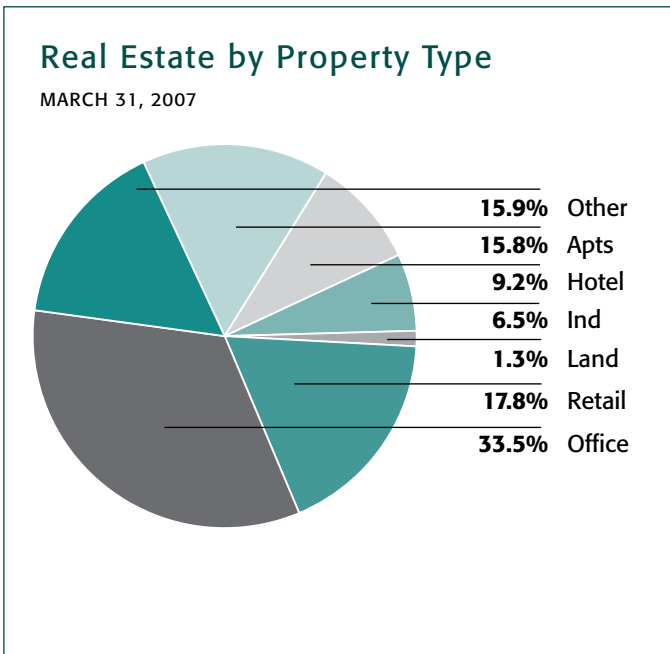
As of June 30, 2007, the carrying value of the program was approximately \$3.6 billion. The vast majority of the program is invested in limited partnerships. Sectors in which the program invests include leveraged buyouts, venture capital, growth, sub-debt, distressed, energy and special situations. The breakdown of the Private Equity Program's market value by sub-class was as follows:



Real Estate

A portion of the portfolio is invested in real estate to help diversify the total fund by providing exposure to an asset class that has a low correlation with the public markets. Real estate produced a 23.8% return for the fiscal year, outperforming its benchmark by 460 basis points.

Over the course of the year, the percentage of the total fund represented by the real estate portfolio increased from 4.7% to 5.1% due primarily to reinvested income and appreciation. At fiscal year end, the composition of the portfolio was composed of approximately 23% public real estate (mostly REITS) and 77% in private assets. Portfolio leverage as a percentage of total real estate assets was 41.0% as of June 30, 2007.



The VRS fund is dedicated to the financial security of members, retirees and their beneficiaries. Thanks to the hard work of the investment team, the fund earned nearly \$10 billion during the fiscal year, bringing it to \$58.3 billion at June 30, 2007.



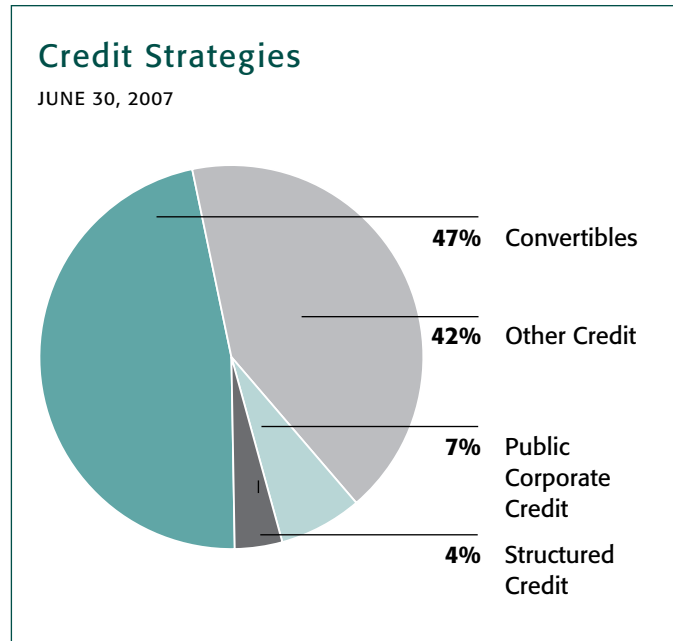
Credit Strategies

The expectation for this program is that it will produce returns comparable to the long-term expectations for domestic equities, while providing higher levels of current income, lower volatility and diversification benefits to the plan.

Common elements of credit strategies investments are that they tend to contain risks associated with credit markets (credit, structure, liquidity). They also tend to produce a higher level of current income relative to equity investments. Some examples of investments within this program include public high yield debt, private high yield debt, bank loans, emerging markets debt, structured credit long/short credit and convertible securities.

The program's return for the fiscal year was 13.6%, while the Credit Strategies benchmark returned 13.5%. For purposes of evaluating the relative return of the program, the fiscal year had two distinct periods. The vast majority of the year experienced strong returns in credit related products. During this period, the VRS portfolio lagged the benchmark due to its diversified composition and emphasis on a relatively stronger portfolio from a fundamental quality standpoint. At the end of the fiscal year, however, the markets struggled as credit concerns and risk aversion reemerged.

During the month of June, when this event began to unfold, the VRS portfolio outpaced the benchmark.



MORE INFORMATION

A complete list of the investment portfolio is available on request. Address requests to the Chief Investment Officer of the Virginia Retirement System, P.O. Box 2500, Richmond, VA 23218-2500.

VRS Money Managers

The diversified investment structure as of June 30, 2007 is reflected in the following tables, which list VRS managers by investment program and style.

Public Equity Money Managers

External	Style Description
Acadian Asset Management	Non-U.S. Small & Emerging Markets
AllianceBernstein	Global
Aronson + Johnson + Ortiz	U.S. Small & U.S. Large
Arrowstreet Capital	Global
Ashmore Investment Management	Emerging Markets
BlackRock	Non-U.S. Small
Barclays Global Investors	U.S. Large & Active Currency
Capital Guardian Trust Company	Global
First Quadrant	Active Currency
Freeman Associates Investment Management	U.S. Large
Grantham, Mayo and Van Otterloo & Company	Non-U.S. Small
J. P. Morgan Investment Management	U.S. Large
Lee Overlay Partners	Active Currency
LSV Asset Management	Non-U.S. Small
Relational Investors	U.S. Large
Russell Investment Group	U.S. Large
Select Equity Group	U.S. Small
Shamrock Capital Advisors	U.S. Small
State Street Global Advisors	U.S. Large & Non-U.S. Large
Symphony Asset Management	U.S. Large
T. Rowe Price	Emerging Markets & Global
The Boston Company	Emerging Markets
TimesSquare Capital Management	U.S. Small
Wellington Management	Global
Internal	Style Description
Afton	U.S. Small
Madison	U.S. Large
Potomac Core	U.S. Large
Russell 2000 Synthetic	U.S. Small
York	U.S. Large
Hedge Funds – Top 10 Managers	Style Description
Blue Ridge, LP	Equity Long/Short
Ironbound Partners Overseas, Ltd.	Equity Long/Short
New Mountain	Equity Long/Short
ValueAct Capital	Equity Long/Short
TPG-Axon Partners (Overshore), Ltd.	Equity Long/Short
Glenhill Capital	Equity Long/Short
Jana Offshore Partners Ltd.	Equity Long/Short
Deephaven Capital Management, LP	Multi-Strategy
Clovis Capital Partners	Equity Long/Short
Seneca Capital International, Ltd.	Multi-Strategy

Fixed Income Managers

External	Style Description
Agincourt	Core/External Active
BlackRock	Core/External Active
Prudential	Core/External Active
Smith Breeden	Core/External Active
Wellington	Core/External Active
Western Asset Management	Core/External Active
State Street Global Advisors	External Passive
VRS Internal	Internal Risk Controlled

Private Equity – Top 10 Managers

	Style Description
Welsh, Carson, Anderson and Stowe	Buyout and Sub-Debt
Hellman and Friedman	Buyout
Madison Dearborn	Buyout
Apax	International Buyout
TA Associates	Growth and Sub-Debt
Nordic Capital	International Buyout
First Reserve	Energy
Texas Pacific Group	Buyout
Summit Partners	Growth and Sub-Debt
Charterhouse	International Buyout

Credit Strategy Managers

	Style Description
Anchorage Advisors, LLC	Long Short Credit
Babson Capital	Mezzanine Credit
BlackRock Kelso Capital	Bank Loans and Mezzanine Credit
Hyperion Brookfield Asset Management	Structured Credit
Oaktree Capital Management	Mezzanine Credit and Convertibles
Post Advisory Group	High Yield Credit and Bank Loans
Prudential	High Yield Credit and Mezzanine Credit
Stone Harbor Investment Partners	Public High Yield Credit
Seix Advisors	Public High Yield Credit
Zazove Associates	Convertibles

Real Estate Managers

Public Real Estate Securities	Style Description
ING Clarion Real Estate Securities	REIT Portfolio
Internal - Monroe	REIT Portfolio
Urdang Securities Management, Inc.	REIT Portfolio
Wellington Management Company, LLP	REIT Portfolio
Private Real Estate	Style Description
Morgan Stanley	Core
JP Morgan Asset Management	Core
AvalonBay Communities, Inc.	Enhanced Core
CIM Group	Enhanced Core
Liquid Realty Partners	Enhanced Core
ProLogis	Enhanced Core
Prudential Real Estate Investors	Enhanced Core
Security Capital European Realty	Enhanced Core
TA Associates Realty	Enhanced Core
AMB Investment Management, Inc.	Opportunistic
Blackstone Real Estate Partners	Opportunistic
Capmark Investments	Opportunistic
Colonnade Properties	Opportunistic
Hines	Opportunistic
JER Partners	Opportunistic
Koll Bren Schreiber	Opportunistic
Lazard Frères Real Estate Investors	Opportunistic
Oaktree Capital Management	Opportunistic

Public Equity Commissions

JULY 1, 2006 THROUGH JUNE 30, 2007

Broker	Commission	Broker	Commission
Investment Tech Group, Inc.	\$ 2,287,892	Credit Lyonnais	\$ 485,539
Goldman, Sachs & Co.	2,125,988	Societe Generale	466,718
Deutsche Bank Securities	1,996,557	Pershing	374,552
Bank of America Montgomery	1,591,744	J. P. Morgan/Robert Fleming	320,976
Merrill Lynch, Pierce, FE	1,465,453	ABN AMRO	262,879
CSFB LLC NY	1,357,770	Brockhouse & Cooper, Inc.	253,141
Citigroup Global Markets	1,183,875	Daiwa Securities America	242,338
Lehman Brothers, Inc., New York	1,130,315	B Trade Svcs., LLC, New York	199,871
Instinet Corp.	1,117,365	MacQuarie Equities, Ltd., Sydney	180,142
Jeffries & Co., Inc.	950,458	Liquidnet, Inc.	158,079
Morgan Stanley & Co., Inc.	907,358	Dresdner Kleinwort Securities, LLC, New York	109,251
Bear Stearns Securities Co., Inc.	865,185	Calyon Securities, New York	108,385
UBS Securities, LLC	848,231	Other Brokers	784,505
Nomura Securities	797,854		
Total FY 2007			\$ 22,572,421

Schedule of Investment Management Fees and Expenses for the Year Ended June 30, 2007

(EXPRESSED IN THOUSANDS)

	Assets Under Management *	Management Fees and Expenses
External Management:		
Domestic Managers	\$ 8,737,171	\$ 30,483
Non-U.S. Equity Managers	8,311,424	31,398
Global Equity Managers	6,293,882	20,099
Fixed Income Managers	14,364,742	7,606
Credit Strategies Managers	1,797,584	18,896
Real Estate Managers	2,583,818	23,247
Alternative Investment Managers	3,682,446	72,007
Hedge Funds Managers	2,604,569	33,290
Internal Management	10,886,695	11,438
Miscellaneous Fees and Expenses:		
Custodian Fees	—	4,146
Legal Fees	—	122
Other Fees and Expenses	—	585
Total	\$ 59,262,331	\$ 253,317

* Does not include short-term investments managed by the Treasury of Virginia and the VRS Master Custodian.

Investment Summary

In accordance with Section 51.1-124.31 of the *Code of Virginia* (1950), as amended, the Board of Trustees has pooled substantially all assets of the Virginia Retirement System, the State Police Officers' Retirement System, the Virginia Law Officers' Retirement System, the Judicial Retirement System, the Group Life Insurance Fund, the Retiree Health

Insurance Credit Fund and the Disability Insurance Trust Fund into a common investment pool. The common investment pool of the pension trust funds and other trust funds held the following composition of investments at June 30, 2007 and 2006 (in thousands):

	2007 Fair Value	Percent of Total Value	2006 Fair Value	Percent of Total Value
Bonds and Mortgage Securities				
U. S. Government and Agencies	\$ 3,107,820	5.19%	\$ 2,939,665	5.97%
Mortgage Securities	5,199,395	8.68%	3,651,298	7.42%
Corporate and Other Bonds	6,606,861	11.03%	3,860,804	7.85%
Total Bonds and Mortgage Securities	14,914,076	24.90%	10,451,767	21.24%
Common and Preferred Stocks	24,176,918	40.38%	16,377,422	33.30%
Index and Pooled Funds				
Equity Index and Pooled Funds	12,656,822	21.14%	14,501,774	29.48%
Fixed Income Commingled Funds	1,248,250	2.08%	2,166,851	4.41%
Total Index and Pooled funds	13,905,072	23.22%	16,668,625	33.89%
Real Estate				
Private Real Estate	2,583,818	4.31%	1,524,935	3.10%
Private Equity	3,682,446	6.15%	2,708,592	5.51%
Short-Term Investments				
Treasurer of Virginia - LGIP Investment Pool	147,817	0.25%	73,407	0.15%
TBC Pooled Employee Trust Fund	394,867	0.66%	1,321,106	2.69%
Foreign Currencies	78,083	0.13%	60,947	0.12%
Total Short-Term Investments	620,767	1.04%	1,455,460	2.96%
Total Investments	\$ 59,883,097	100.00%	\$ 49,186,801	100.00%

Actuarial Section

Actuary's Certification Letter

Solvency Test

Schedule of Active Member Valuation Data

Schedule of Retiree and Beneficiary Valuation Data

Analysis of Actuarial Gains and Losses

Analysis of Changes in Allowances for Retirees and
Beneficiaries

Summary of Actuarial Assumptions and Methods

Summary of Benefit Plan Provisions

Summary of Plan Changes



...to the right customer...

The VRS membership grew 3.6% in fiscal year 2007, from 562,459 in FY 2006 to 582,469 in FY 2007. At June 30, 2007, the active membership included:

- 80,262 state employees
- 145,122 teachers
- 101,461 employees of participating political subdivisions
- 1,885 state police officers
- 10,061 other Virginia law officers
- 424 judges.

In addition, the VRS membership included 130,500 retirees at June 30, 2007. Since 1998, the number of retirees has increased almost 50%.

Actuary Letter

Wachovia Bank, N.A.
Wachovia Retirement Services
VA9412
9020 Stony Point Parkway, Suite 200
Richmond, VA 23235

Tel 804 267-3100
Fax 804 330-1386

WACHOVIA

July 6, 2007

Board of Trustees
Virginia Retirement System
P.O. Box 2500
Richmond, VA 23218-2500

June 30, 2006 Actuarial Valuation Report

Dear Members of the Board:

We are pleased to present the actuarial valuation results for the following retirement plans of the Virginia Retirement System (VRS):

- VRS (state employees, teachers, employees of participating political subdivisions)
- State Police Officers' Retirement System (SPORS)
- Virginia Law Officers' Retirement System (VaLORS)
- Judicial Retirement System (JRS)

We certify the information contained in this report is accurate and fairly presents the actuarial status of the retirement plans as of June 30, 2006. The valuation reflects the benefits in effect on the valuation date and was prepared on the basis of the data submitted by the VRS.

Participant Data and Assets

The individual data for members of the system as of the valuation date was reported to the actuary by the VRS. While we did not verify the individual records, we did perform tests for internal consistency and reasonableness in relation to the data submitted for the prior year's valuation.

The balance of current assets in the trust fund taken into account for the valuation was based on statements prepared for us by the VRS staff. We did not perform any type of audit on the plan assets.

Actuarial Assumptions and Methods

The actuarial cost method utilized is the entry age normal cost method. This method is an acceptable method for determining the annual required contribution in accordance with GASB statements 25 and 27. For the purpose of determining contribution rates, the excess (shortfall) between expected and actual investment income is recognized over a five-year period, with the restriction that the actuarial asset value cannot be less than 80% or more than 120% of market value.

Legislative Changes

There were no legislative changes during the fiscal year ending June 30, 2006, which had a financial impact on the retirement plans.

Actuarial Schedules

The following schedules (or updates to them) were prepared by VRS from information provided by us during the 2006 actuarial valuation and supplemental information provided by us. We have reviewed them for inclusion in the 2007 Comprehensive Annual Financial Report.

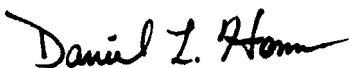
- Schedule of Funding Progress
- Summary of Actuarial Assumptions and Methods
- Solvency Test
- Schedule of Active Member Valuation Data
- Schedule of Retirees and Beneficiaries
- Analysis of Actuarial Gains and Losses
- Schedules of Selected Experience Rates

Actuarial Certification

To the best of our knowledge, this report is complete and accurate. All costs and liabilities have been determined in conformity with generally accepted actuarial principles and with the Actuarial Standards of Practice issued by the Actuarial Standards Board. In our opinion, we believe the assumptions used are individually reasonable and represent the best estimate of anticipated experience under the VRS. The undersigned are available to answer questions regarding this report.

Respectfully submitted,

Wachovia Retirement Services



Daniel L. Homan, EA, MAAA
Senior Consultant



Alice C. Hicks, ASA, EA, MAAA
Consultant

Solvency Test

(EXPRESSED IN THOUSANDS)

Valuation Date (June 30)	Aggregate Accrued Liabilities for				Portion of Accrued Liabilities Covered by Assets		
	(1) Active Member Contributions	(2) Retirees and Beneficiaries	(3) Active Members*	Valuation Assets	(1)	(2)	(3)
VIRGINIA RETIREMENT SYSTEM (VRS)							
2006	\$ 6,988,172	\$ 23,055,815	\$ 22,777,916	\$ 42,668,752	100.00%	100.00%	55.43%
2005	6,555,402	21,140,882	21,932,204	40,372,648	100.00%	100.00%	57.80%
2004	6,139,908	18,971,864	18,846,578	39,691,562	100.00%	100.00%	77.36%
2003	5,703,557	17,223,070	17,770,944	39,242,624	100.00%	100.00%	91.81%
2002	5,285,338	15,878,494	17,101,328	38,957,256	100.00%	100.00%	104.05%
2001	4,847,656	14,411,943	16,119,211	37,967,820	100.00%	100.00%	116.06%
2000	4,639,007	12,652,663	15,350,685	34,392,303	100.00%	100.00%	111.40%
1999	4,240,017	11,820,608	15,358,116	29,803,990	100.00%	100.00%	89.49%
1998	3,937,941	10,732,243	14,359,783	25,480,634	100.00%	100.00%	75.28%
1996	3,202,232	9,213,095	11,426,575	19,031,780	100.00%	100.00%	57.90%
STATE POLICE OFFICERS' RETIREMENT SYSTEM (SPORS)							
2006	\$ 66,055	\$ 378,636	\$ 285,236	\$ 538,646	100.00%	100.00%	32.94%
2005	62,917	337,017	273,239	514,330	100.00%	100.00%	41.87%
2004	61,529	310,306	284,509	510,604	100.00%	100.00%	48.77%
2003	59,097	277,282	279,243	508,576	100.00%	100.00%	61.67%
2002	57,152	253,687	283,797	507,889	100.00%	100.00%	69.43%
2001	54,507	215,658	286,463	494,952	100.00%	100.00%	78.47%
2000	50,044	199,822	262,761	440,903	100.00%	100.00%	72.70%
1999	45,516	200,288	217,252	376,780	100.00%	100.00%	60.29%
1998	42,154	190,196	192,348	321,696	100.00%	100.00%	46.45%
1996	37,715	139,258	193,888	243,066	100.00%	100.00%	34.10%
VIRGINIA LAW OFFICERS' RETIREMENT SYSTEM (VaLORS)**							
2006	\$ 156,310	\$ 412,767	\$ 527,291	\$ 656,668	100.00%	100.00%	16.61%
2005	148,890	330,502	500,705	575,327	100.00%	100.00%	19.16%
2004	143,836	246,872	536,424	508,561	100.00%	100.00%	21.97%
2003	135,144	195,554	523,138	457,615	100.00%	100.00%	24.26%
2002	127,975	110,426	567,716	418,518	100.00%	100.00%	31.73%
2001	111,143	5,639	510,857	392,815	100.00%	100.00%	54.03%
2000	108,538	27,356	543,943	307,301	100.00%	100.00%	31.51%
JUDICIAL RETIREMENT SYSTEM (JRS)							
2006	\$ 34,756	\$ 240,005	\$ 149,637	\$ 302,734	100.00%	100.00%	18.69%
2005	32,143	229,942	140,216	287,825	100.00%	100.00%	18.36%
2004	30,176	211,228	124,171	285,178	100.00%	100.00%	35.25%
2003	28,766	198,005	121,265	282,326	100.00%	100.00%	45.81%
2002	28,089	186,886	137,029	281,056	100.00%	100.00%	48.22%
2001	23,595	176,142	142,095	276,542	100.00%	100.00%	54.05%
2000	24,079	191,146	115,127	244,721	100.00%	100.00%	25.62%
1999	20,978	171,136	110,328	209,992	100.00%	100.00%	16.20%
1998	19,239	152,557	102,629	179,693	100.00%	100.00%	7.69%
1996	16,885	140,964	84,918	137,886	100.00%	85.80%	0.00%

* Employer-financed portion.

** The Virginia Law Officers' Retirement System went into effect October 1, 1999.

Aggregate Accrued Liabilities are determined under the entry age normal cost method (System-funded method used to determine employer contribution requirements).

The progress of a retirement system in accumulating assets to pay benefits when due can be measured by examining the extent to which assets accumulated for benefits cover 1) active member contributions to the system; 2) liabilities for future benefits to retirees and beneficiaries; and 3) liabilities for the employer-financed portion of service already rendered by active members. In a system receiving actuarially determined employer contributions, the liabilities for member contributions and future benefits to retirees and beneficiaries will generally be fully covered by accumulated assets. In addition, the liabilities for service already rendered will be partially covered by the remainder of the accumulated assets and will increase over time.

Actuarial Assumptions and Methods	1996	1998/1999	2000/2001	2002/2003/2004	2005/2006
Valuation interest rate	8.0%	8.0%	8.0%	8.0%	7.5%
Salary scale inflation factor	4.0%	4.0%	3.0%	3.0%	2.5%
Change in decremental assumptions	Yes	No	Yes	No	Yes
Value of ancillary benefits included	Yes	Yes	Yes	Yes	Yes
Value of post-retirement adjustments to date included	Yes	Yes	Yes	Yes	Yes
Assets valued at	Modified Market	Modified Market	Modified Market	Modified Market	Modified Market

Schedule of Active Member Valuation Data

Valuation Date (June 30)	Active Members				
	Number	Annual Payrolls (000s)	Average Annual Pay	Annualized % Increase in Average Pay	Number of Employers
VIRGINIA RETIREMENT SYSTEM (VRS)					
2006	320,065	\$ 13,001,551	\$ 40,622	4.1%	575
2005	312,981	12,212,145	39,019	3.5%	571
2004	305,388	11,509,902	37,689	4.1%	565
2003	300,612	10,884,629	36,208	1.1%	559
2002	297,921	10,668,980	35,811	2.9%	551
2001	291,621	10,145,212	34,789	3.9%	551
2000	284,486	9,528,666	33,494	4.7%	545
1999	285,596	9,138,060	31,996	2.7%	532
1998	277,223	8,638,414	31,161	6.2%	519
1996	264,656	7,769,043	29,355	5.9%	513
STATE POLICE OFFICERS' RETIREMENT SYSTEM (SPORS)					
2006	1,795	\$ 93,742	\$ 52,224	4.1%	1
2005	1,811	90,865	50,174	7.3%	1
2004	1,755	82,100	46,781	2.2%	1
2003	1,727	79,020	45,756	(1.3%)	1
2002	1,740	80,680	46,368	(1.5%)	1
2001	1,771	83,339	47,058	2.7%	1
2000	1,768	80,977	45,801	5.3%	1
1999	1,761	76,628	43,514	11.9%	1
1998	1,682	65,427	38,898	4.7%	1
1996	1,604	59,599	37,156	3.2%	1
VIRGINIA LAW OFFICERS' RETIREMENT SYSTEM (VaLORS)*					
2006	9,904	\$ 320,869	\$ 32,398	3.8%	1
2005	9,819	306,574	31,222	2.0%	1
2004	9,746	298,313	30,609	1.0%	1
2003	9,626	291,801	30,314	(0.6%)	1
2002	10,036	306,024	30,493	(0.7%)	1
2001	10,434	320,254	30,693	2.7%	1
2000	10,542	315,158	29,895	0.0%	1
JUDICIAL RETIREMENT SYSTEM (JRS)					
2006	415	\$ 54,289	\$ 130,818	4.4%	1
2005	414	51,874	125,300	5.1%	1
2004	405	48,271	119,188	2.2%	1
2003	408	47,568	116,588	0.0%	1
2002	408	47,568	116,588	0.0%	1
2001	404	47,125	116,646	2.5%	1
2000	399	45,394	113,769	6.7%	1
1999	390	41,590	106,641	3.8%	1
1998	383	39,332	102,695	8.5%	1
1996	378	35,783	94,664	4.7%	1

* The Virginia Law Officers' Retirement System went into effect on October 1, 1999.

Schedule of Retiree and Beneficiary Valuation Data

Valuation Date (June 30)	Retirees and Beneficiaries				
	Retirees and Beneficiaries Added/Removed*	Total Retirees and Beneficiaries	Annual Allowances (000)s	Annualized % Increase in Annual Allowances	Average Annual Allowances
VIRGINIA RETIREMENT SYSTEM (VRS)					
2006	8,949/3,834	121,786	\$ 1,972,394	8.7%	\$ 16,196
2005	9,151/4,250	116,671	1,814,791	8.3%	15,555
2004	7,913/2,561	111,770	1,676,175	9.0%	14,997
2003	7,920/3,554	106,418	1,537,902	11.8%	14,452
2002	7,451/3,496	102,052	1,375,777	6.7%	13,481
2001	7,962/3,337	98,097	1,289,657	12.1%	13,147
2000	7,932/3,685	93,472	1,150,213	8.6%	12,305
1999		89,225	1,059,602	16.4%**	11,786
1998		88,500	896,409	3.4%	10,129
1996		80,499	838,147	8.9%	10,412
STATE POLICE OFFICERS' RETIREMENT SYSTEM (SPORS)					
2006	57/23	957	\$ 31,394	7.6%	\$ 32,805
2005	70/9	923	29,186	10.7%	31,620
2004	56/4	862	26,361	11.1%	30,581
2003	63/25	810	23,737	18.2%	29,305
2002	72/12	772	20,077	7.1%	26,006
2001	26/11	712	18,748	8.0%	26,331
2000	38/8	697	17,362	9.9%	24,910
1999		667	15,793	23.2%**	23,678
1998		668	12,844	15.1%	19,227
1996		572	9,865	14.5%	17,247
VIRGINIA LAW OFFICERS' RETIREMENT SYSTEM (VaLORS)***					
2006	209/34	1,381	\$ 31,849	16.7%	\$ 23,062
2005	248/12	1,206	27,286	33.6%	22,625
2004	207/2	970	20,423	27.8%	21,055
2003	245/10	765	15,982	72.7%	20,892
2002	251/18	527	9,252	324.2%	17,556
2001	197/13	294	2,181	198.8%	7,418
2000	124/14	110	730	0.0%	6,636
JUDICIAL RETIREMENT SYSTEM (JRS)					
2006	25/21	399	\$ 24,905	4.9%	\$ 62,420
2005	25/17	395	23,736	8.9%	60,092
2004	33/21	387	21,789	6.4%	56,302
2003	35/26	375	20,488	8.3%	54,635
2002	14/17	366	18,918	1.2%	51,689
2001	21/16	369	18,699	7.6%	50,675
2000	21/9	364	17,373	4.3%	47,728
1999		352	16,659	11.1%**	47,327
1998		347	14,787	4.1%	42,615
1996		330	13,666	12.4%	41,412

* Number of retirees and beneficiaries added and removed is unavailable prior to FY 2000.

** Increase in annual allowances due to 2% ad hoc increase in retiree benefit allowances effective January 1, 1999 and an increase in the benefit formula multiplier.

*** The Virginia Law Officers' Retirement System went into effect on October 1, 1999.

Analysis of Actuarial Gains and Losses for the Year Ended June 30, 2006

(EXPRESSED IN THOUSANDS)

	VRS	SPORS	VaLORS	JRS	Total
A. Calculation of Expected Unfunded Actuarial Accrued Liability (UAAL)					
1. UAAL as of June 30, 2005	\$ 9,254,402	\$ 158,843	\$ 404,770	\$ 114,476	\$ 9,932,491
2. Normal Cost for Previous Year	1,113,664	11,327	40,038	15,298	1,180,327
3. Actual Contributions During the Year	(1,458,836)	(20,189)	(68,688)	(18,966)	(1,566,679)
4. Interest at Previous Year's Rate of 7.50%					
a. On UAAL	694,080	11,913	30,358	8,586	744,937
b. On Normal Cost	83,524	850	3,003	1,147	88,524
c. On Contributions	(54,706)	(757)	(2,576)	(711)	(58,750)
d. Total	722,898	12,006	30,785	9,022	774,711
5. Expected UAAL as of June 30, 2006 (A1 + A2 + A3 + A4)	9,632,128	161,987	406,905	119,830	10,320,850
6. Actual UAAL as of June 30, 2006	10,515,245	191,281	439,700	121,664	11,267,890
7. Total Gain/(Loss) (A5 - A6)	(883,117)	(29,294)	(32,795)	(1,834)	(947,040)
B. Calculation of Asset Gain/(Loss)					
1. Actual Value of Assets (AVA) as of June 30, 2005	40,370,244	514,330	575,327	287,825	41,747,726
2. Contributions During the Year	1,458,836	20,189	68,688	18,966	1,566,679
3. Benefit Payments During the Year	(2,101,360)	(32,904)	(34,033)	(24,717)	(2,193,014)
4. Interest at Previous Year's Rate of 7.50%					
a. On AVA at Beginning of Year	3,027,769	38,575	43,150	21,587	3,131,081
b. On Contributions	54,706	757	2,576	711	58,750
c. On Benefit Payments	(78,801)	(1,234)	(1,276)	(927)	(82,238)
d. Total	3,003,674	38,098	44,450	21,371	3,107,593
5. Expected AVA as of June 30, 2006 (B1 + B2 + B3 + B4)	42,731,394	539,713	654,432	303,445	44,228,984
6. Actual AVA as of June 30, 2006	42,668,752	538,646	656,668	302,734	44,166,800
7. Total Gain/(Loss) on Assets (B6 - B5)	(62,642)	(1,067)	2,236	(711)	(62,184)
C. Calculation of Liability Gain/(Loss)					
1. Gain/(Loss) due to Changes in Actuarial Assumptions	(22,190)	(4,294)	(10,049)	-	(36,533)
2. Gain/(Loss) due to Plan Amendments	-	-	-	-	-
3. Liability Experience Gain/(Loss) (A7-B7-C1-C2)	\$ (798,285)	\$ (23,933)	\$ (24,982)	\$ (1,123)	\$ (848,323)

Analysis of Changes in Allowances for Retirees and Beneficiaries

(EXPRESSED IN THOUSANDS)

Valuation Date (June 30)	Beginning Annual Allowance	Additions**	Reductions	Ending Annual Allowance
VIRGINIA RETIREMENT SYSTEM (VRS)				
2006	\$ 1,814,791	\$ 190,775	\$ 33,172	\$ 1,972,394
2005	1,676,175	187,247	48,631	1,814,791
2004*	1,537,902	167,577	29,304	1,676,175
STATE POLICE OFFICERS' RETIREMENT SYSTEM (SPORS)				
2006	\$ 29,186	\$ 2,378	\$ 170	\$ 31,394
2005	26,361	3,035	210	29,186
2004*	23,737	2,717	93	26,361
VIRGINIA LAW OFFICERS' RETIREMENT SYSTEM (VaLORS)				
2006	\$ 27,286	\$ 4,692	\$ 129	\$ 31,849
2005	20,423	7,541	678	27,286
2004*	15,982	4,554	113	20,423
JUDICIAL RETIREMENT SYSTEM (JRS)				
2006	\$ 23,736	\$ 1,983	\$ 814	\$ 24,905
2005	21,789	2,017	70	23,736
2004*	20,488	1,387	86	21,789

* Details of changes in allowances is unavailable prior to FY 2004.

** Additions to the Annual Allowance include added retirees and the annual cost-of-living adjustment (COLA) provided to current retirees and beneficiaries.

Summary of Actuarial Assumptions and Methods

The VRS Board of Trustees adopted the following actuarial assumptions and methods on May 19, 2005 on the recommendation of its actuary. These assumptions were based on an analysis of plan experience for the five-year period of July 1, 1999 through June 30, 2004. These assumptions were used for the June 30, 2005 and June 30, 2006 actuarial valuations.

INVESTMENT RETURN RATE

7.50% per annum, compounded annually, composed of an assumed 2.50% inflation rate and a 5.00% real rate of return. Benefits are assumed to increase by 2.50% annually due to the COLA.

MORTALITY RATES

Virginia Retirement System, State Police Officers' Retirement System, Virginia Law Officers' Retirement System and Judicial Retirement System.

Pre-Retirement

1994 Group Annuity Mortality Table for males and females with a one-year set back in age for males and females in all employer groups.

Post-Retirement

1994 Group Annuity Mortality Table for males and females with a one-year set back in age for male and female state employees and employees of political subdivisions not receiving enhanced hazardous duty benefits; a three-year set back in age for male and female teachers; and a one-year set back in age for male and female judges.

1994 Group Annuity Mortality Table for males and females with a four-year set back in age for state police officers, employees of political subdivisions in hazardous duty positions receiving enhanced benefits and other Virginia law enforcement and correctional officers.

Post-Disablement

70% of PBGC Disabled Mortality Table 5a for males; 90% of PBGC Disabled Mortality Table 6a for females.

Retirement Rates

State Employees and Employees of Political Subdivisions not Receiving Enhanced Hazardous Duty Benefits

Sample rates of retirement are shown below for members eligible to retire.

RETIREMENT PER 100 MEMBERS				
Age	Retirement with Less Than 30 Years of Service		Retirement with 30 or More Years of Service	
	Male	Female	Male	Female
50	3.0	3.0	10.0	10.0
55	5.0	5.0	10.0	10.0
59	5.0	5.0	10.0	10.0
60	5.0	7.5	15.0	15.0
61	10.0	10.0	20.0	20.0
62	15.0	15.0	30.0	30.0
64	15.0	20.0	25.0	20.0
65	—	—	35.0	45.0
67	—	—	30.0	30.0
70	—	—	100.0	100.0

Teachers

Sample rates of retirement are shown below for members eligible to retire.

RETIREMENT PER 100 MEMBERS				
Age	Retirement with Less Than 30 Years of Service		Retirement with 30 or More Years of Service	
	Male	Female	Male	Female
50	2.0	2.0	20.0	20.0
55	5.0	5.0	22.5	25.0
59	7.0	8.0	22.5	30.0
60	10.0	10.0	25.0	30.0
61	10.0	10.0	25.0	25.0
62	20.0	20.0	40.0	40.0
64	15.0	15.0	30.0	30.0
65	—	—	40.0	40.0
67	—	—	30.0	30.0
70	—	—	100.0	100.0

State Police Officers, Employees of Political Subdivisions in Hazardous Duty Positions Receiving Enhanced Benefits and Virginia Law Officers

Sample rates of retirement are shown below for members eligible to retire.

RETIREMENT PER 100 MEMBERS		
Age	Reduced Retirement	Unreduced Retirement
50	10.0	20.0
55	10.0	20.0
59	12.0	35.0
60	—	100.0

Judicial Retirement System

Sample rates of retirement are shown below for members eligible to retire.

Age	Rate
At first age eligible for an unreduced retirement benefit	50.0%
At subsequent ages	15.0%
At age 70	100.0%

Disability Rates

As shown below for selected ages.

State Employees and Employees of Political Subdivisions not Receiving Enhanced Hazardous Duty Benefits

14% of disability cases are assumed to be service-related.

DISABILITIES PER 100 MEMBERS		
Age	Male	Female
20	0.030	0.014
30	0.140	0.054
40	0.270	0.122
50	0.510	0.459
60	1.500	1.350

Teachers

5% of disability cases are assumed to be service-related.

DISABILITIES PER 100 MEMBERS		
Age	Male	Female
20	—	—
30	0.013	0.008
40	0.026	0.046
50	0.149	0.163
60	0.422	0.442

State Police Officers, Employees of Political Subdivisions in Hazardous Duty Positions Receiving Enhanced Benefits and Virginia Law Officers

60% of disability cases are assumed to be service-related.

DISABILITIES PER 100 MEMBERS		
Age	Rate	
20	—	
30	0.028	
40	0.210	
50	0.675	
60	—	

Judicial Retirement System

5% of disability cases are assumed to be service-related.

DISABILITIES PER 100 MEMBERS		
Age	Male	Female
20	—	—
30	0.007	0.007
40	0.142	0.090
50	0.480	0.397
60	—	—

Termination Rates

Withdrawal rates are based on age and years of service credit. Sample rates for selected ages and years of service are shown below (for causes other than death, disability or retirement).

State Employees and Employees of Political Subdivisions not Receiving Enhanced Hazardous Duty Benefits

PROBABILITY OF DECREMENT DUE TO WITHDRAWAL

Age	Years of Service – Males					Years of Service – Females				
	1	3	6	9	10+	1	3	6	9	10+
25	0.1883	0.1346	0.0810	0.0498	0.0483	0.2309	0.1755	0.1388	0.0753	0.0586
35	0.1490	0.1064	0.0787	0.0498	0.0368	0.1708	0.1336	0.1002	0.0668	0.0432
45	0.1143	0.0762	0.0642	0.0407	0.0214	0.1315	0.0953	0.0718	0.0490	0.0240
55	0.0975	0.0596	0.0399	0.0260	0.0134	0.1155	0.0734	0.0476	0.0279	0.0121

Teachers

PROBABILITY OF DECREMENT DUE TO WITHDRAWAL

Age	Years of Service – Males					Years of Service – Females				
	1	3	6	9	10+	1	3	6	9	10+
25	0.1758	0.1234	0.0565	0.0384	0.0804	0.1413	0.1316	0.0953	0.1114	0.1241
35	0.1585	0.0989	0.0567	0.0381	0.0350	0.1416	0.1165	0.0836	0.0618	0.0439
45	0.1391	0.0782	0.0480	0.0312	0.0146	0.1161	0.0793	0.0561	0.0365	0.0176
55	0.1419	0.0726	0.0322	0.0187	0.0093	0.1161	0.0665	0.0385	0.0246	0.0090

State Police Officers, Employees of Political Subdivisions in Hazardous Duty Positions Receiving Enhanced Benefits and Virginia Law Officers

PROBABILITY OF DECREMENT DUE TO WITHDRAWAL

Age	Years of Service – Males					Years of Service – Females				
	1	3	6	9	10+	1	3	6	9	10+
25	0.0854	0.0803	0.0728	0.0299	0.0360	0.1332	0.1047	0.1023	0.0543	0.0438
35	0.0936	0.0773	0.0515	0.0323	0.0248	0.1437	0.0996	0.0671	0.0599	0.0608
45	0.1022	0.0722	0.0438	0.0293	0.0141	0.1172	0.0984	0.0770	0.0639	0.0591
55	0.1149	0.0719	0.0417	0.0224	0.0098	0.0573	0.1023	0.1289	0.0671	0.0411

Judicial Retirement System

There are no assumed rates of withdrawal prior to service retirement (for causes other than death, disability or retirement).

Salary Increase Rates

The sample salary increase rates are shown below.

State Employees and Employees of Political Subdivisions not Receiving Enhanced Hazardous Duty Benefits

Inflation rate of 2.50% plus productivity component of 1.25% plus step-rate/promotional component as shown. It is assumed state employees covered under the Virginia Sickness and Disability Program (VSDP) receive a 3.75% annual increase in pay while disabled and this adjusted pay is used to determine deferred retirement benefits payable from the System.

Years of Service	Annual Step-Rate/Promotional Rates of Increase	Total Annual Rate of Increase
1	1.85%	5.60%
3	1.25%	5.00%
6	0.95%	4.70%
9	0.50%	4.25%
11	0.15%	3.90%
15	0.15%	3.90%
19	0.15%	3.90%
20 or more	—	3.75%

Teachers

Inflation rate of 2.50% plus productivity component of 1.25% plus step-rate/promotional component as shown.

Years of Service	Annual Step-Rate/Promotional Rates of Increase	Total Annual Rate of Increase
1	2.45%	6.20%
3	2.35%	6.10%
6	1.95%	5.70%
9	1.85%	5.60%
11	1.35%	5.10%
15	1.15%	4.90%
19	0.95%	4.70%
20 or more	—	3.75%

Salary Increase Rates, continued

State Police Officers, Employees of Political Subdivisions in Hazardous Duty Positions Receiving Enhanced Benefits and Virginia Law Officers

Inflation rate of 2.50% plus productivity component of 1.00% plus step-rate/promotional component as shown. It is assumed state police and Virginia law officers covered under the Virginia Sickness and Disability Program (VSDP) receive a 3.50% annual increase in pay while disabled and this adjusted pay is used to determine deferred retirement benefits payable from the System.

Years of Service	Annual Step-Rate/Promotional Rates of Increase	Total Annual Rate of Increase
1	1.25%	4.75%
3	1.25%	4.75%
6	0.90%	4.40%
9	0.90%	4.40%
11	0.50%	4.00%
15	0.50%	4.00%
19	0.50%	4.00%
20 or more	—	3.50%

Judicial Retirement System

Salary increase rates are 3.50%.



Political subdivisions may elect to provide enhanced hazardous duty benefits to full-time firefighters, law enforcement officers, emergency medical technicians and jail officers. VRS-covered sheriffs, state police officers and other Virginia law officers also are eligible for enhanced hazardous duty benefits.

Percent Electing a Deferred Termination Benefit

(EXCLUDES JUDICIAL RETIREMENT SYSTEM)

Terminating members are assumed to elect a return of contribution or a deferred annuity, whichever is the most valuable benefit at the time of termination.

Termination benefits are assumed to commence at the first age at which unreduced benefits are available.

Provision for Expense

The assumed investment return represents the anticipated net rate of return after payment of all administrative expenses.

Asset Valuation Method

The actuarial value of assets is equal to the market value of assets less a five-year phase in of the excess (shortfall) between expected investment return and actual income (both based on market value), with the resulting value not being less than 80% or more than 120% of the market value of assets.

Actuarial Cost Method

The funding period required to amortize the unfunded actuarial accrued liability (UAAL) is determined using the Entry Age Normal actuarial cost method. This method assigns the plan's total actuarial present value of future benefits to various periods. The actuarial accrued liability is assigned to years prior to the valuation, and the normal cost is assigned to the year following the valuation. The remaining costs are assigned to future years.

The normal cost rate is determined on an individual basis. The actuarial accrued liability is the difference between the total present value of future benefits and the actuarial present value of future normal costs. The unfunded actuarial accrued liability (UAAL) is the excess of the actuarial accrued liability over the actuarial value of assets.

Payroll Growth Rate

State employees, teachers, state police officers, Virginia law officers and judges: 3.00% based on a zero population growth assumption. Political subdivision employees: 2.50% based on a zero population growth assumption.

Funding Period

State employees, teachers, political subdivision employees, state police officers, Virginia law officers and judges: 20 years closed amortization, computed as a level percent of payroll.

Cost-of-Living Adjustment

2.50% per year compounded annually for the basic benefit. The temporary supplement for state police officers, employees of political subdivisions in hazardous duty positions receiving enhanced benefits and Virginia law officers is assumed to increase at the inflation rate (2.50% per year, compounded annually).

Summary of Benefit Plan Provisions

Retirement Plans

- Virginia Retirement System (VRS), effective March 1, 1952
- State Police Officers' Retirement System (SPORS), effective July 1, 1950
- Judicial Retirement System (JRS), effective July 1, 1970
- Virginia Law Officers' Retirement System (VaLORS), effective October 1, 1999

Plan Year

Twelve-month period ending June 30.

Administration

Plans are administered by the Board of Trustees of the Virginia Retirement System.

Type of Plans

- VRS is a qualified governmental defined benefit retirement plan. For Governmental Accounting Standards Board purposes, it is considered an agent multiple-employer Public Employee/Retirement System (PERS) for participating Virginia cities, counties, towns and political subdivisions, with separate cost-sharing pools for state employees and teachers.
- SPORS is a qualified governmental defined benefit retirement plan. For Governmental Accounting Standards Board purposes, it is considered a single-employer PERS.
- JRS is a qualified governmental defined benefit retirement plan. For Governmental Accounting Standards Board purposes, it is considered a single-employer PERS.
- VaLORS is a qualified governmental defined benefit retirement plan. For Governmental Accounting Standards Board purposes, it is considered a single-employer PERS.

Eligibility

All full-time, salaried permanent employees of the Commonwealth of Virginia and all full-time, salaried permanent employees of local Virginia school boards or any participating Virginia county, city, town or political subdivision are eligible to become members of VRS. All state police officers of the Commonwealth of Virginia are eligible to become members of SPORS. All full-time judges of the Commonwealth of Virginia are eligible to become members of JRS. All full-time, salaried permanent Virginia law enforcement officers and correctional officers other than state police officers are eligible to become members of VaLORS.

Employee Contributions

All active members contribute 5.00% of their creditable compensation per year. The employer may pick up the member's assessment under the provisions of Internal Revenue Code Section 414(h).

Creditable Compensation

Annual salary minus any overtime pay, payments of a temporary nature or payments for extra duties.

Service

Employees, state police officers and Virginia law officers receive credit of one month of service for each month a contribution is made on their behalf to VRS, SPORS and VaLORS. Judges receive credit of one month of service multiplied by a weighting factor of 3.5 (2.5 for judges entering JRS on or after January 1, 1995) for each month a contribution is made to JRS on their behalf. A member also may purchase credit for certain periods, such as time spent in the military, by paying a purchase rate (5% of the larger of current credible compensation or average final compensation times the number of years to be purchased or actuarial cost). Special rules and limits govern the purchase of prior service.

Average Final Compensation

The average of the member's highest 36 consecutive months of creditable compensation.

Normal Retirement

ELIGIBILITY

Members of VRS and JRS may retire under normal retirement on or after age 65 with five years of service credit. A member of SPORS and VaLORS may retire under normal retirement on or after age 60 with five years of service credit.

ANNUAL BENEFIT

For members of VRS and SPORS, 1.7% of average final compensation (AFC) times years of service. Members of VaLORS hired before July 1, 2001 were allowed to make a one-time election to have their benefit based on 2.0% of average annual compensation (AFC) instead of receiving a supplement. For members of JRS, 1.7% of average final compensation (AFC), times years of service, not to exceed 78% of AFC.

SUPPLEMENT

Members of SPORS and employees of political subdivisions in hazardous duty positions receiving enhanced benefits with 20 or more years of service in a hazardous position or with a hire date prior to July 1, 1974 receive an additional allowance payable from the date of retirement to their Social Security normal retirement age. This supplement is adjusted biennially based on increases in Social Security benefits during the interim period. Electing members of VaLORS hired before July 1, 2001 with 20 or more years of service in a hazardous position or with a hire date prior to July 1, 1974 receive an additional allowance payable from the date of retirement to age 65.

PAYMENT FORM

Benefits are paid as a monthly life annuity, with a guarantee that if the payments made do not exceed the member's contributions plus interest, determined as of the date of retirement, the balance will be paid in a lump sum to the member's beneficiary.

Early Retirement

ELIGIBILITY

A member of VRS may retire early after reaching age 50 with credit for 10 years of service, or age 55 with credit for five years of service. Members of SPORS and VaLORS and employees of political subdivisions in hazardous duty positions receiving enhanced benefits may retire early after reaching age 50 with credit for five years of service. A member of JRS may retire early after reaching age 55 with credit for five years of service.

ANNUAL BENEFIT

Calculated the same as the normal retirement benefit using actual service at retirement and multiplied by a reduction factor. No reduction applies if the VRS member has credit for 30 years of service at retirement and is at least age 50 (25 years of service and at least age 50 for members of SPORS and VaLORS and employees of political subdivisions in hazardous duty positions receiving enhanced benefits, and 30 years of service and at least age 60 for members of JRS). For members of VRS and JRS at least age 55 (at least age 50 for members of SPORS and VaLORS and employees of political subdivisions in hazardous duty positions receiving enhanced benefits), the reduction is 0.5% per month for the first 60 months and 0.4% per month for the next 60 months. This reduction is applied for each month the retirement age precedes 65 or, if more favorable, for each month the service at retirement is less than 30 (age 60 with service less than 25 for members of SPORS and VaLORS and employees of political subdivisions in hazardous duty positions receiving enhanced benefits). For VRS members younger than age 55 at retirement, the reduction factor determined as though the member were 55 is further reduced by multiplying it by a second factor, to reflect a 0.6% reduction for each month retirement precedes age 55.

Supplement

ELIGIBILITY

Members of SPORS and employees of political subdivisions in hazardous duty positions receiving enhanced benefits with 20 or more years of service in a hazardous position or with a hire date prior to

July 1, 1974 receive an additional allowance payable annually from the date of retirement to their Social Security normal retirement age. This supplement is adjusted biennially based on increases in Social Security benefits during the interim period. Electing members of VaLORS hired before July 1, 2001 with 20 or more years of service in a hazardous position or with a hire date prior to July 1, 1974 receive an additional allowance payable annually from the date of retirement to age 65.

PAYMENT FORM

Same as for Normal Retirement.

Disability Retirement

ELIGIBILITY

VRS teacher and political subdivision members and JRS members are eligible from the first day of employment. VRS state employees, SPORS and VaLORS members hired prior to January 1, 1999 and who declined coverage under the Virginia Sickness & Disability Program (VSDP) are eligible from the first day of employment.

ANNUAL BENEFIT

Members with less than five years of service credit receive the minimum guaranteed benefit. Members with more than five years of service credit receive the greater of (1) the minimum guaranteed benefit, which is 50% of AFC (66 2/3% if work-related disability) if the member does not qualify for primary Social Security and 33 1/3% of AFC (50% if work-related disability) if the member qualifies for primary Social Security; or (2) 1.7% of AFC times service credit. The work-related benefit is reduced by Worker's Compensation (if any).

SERVICE CREDIT

If a disability occurs before age 60, service is the lesser of (1) twice actual service; or (2) rendered service plus the number of years remaining between the member's age at disability retirement and age 60.

PAYMENT FORM

The disability benefit commences immediately upon the member's retirement. Benefits cease upon recovery or reemployment. Disability benefits are payable as a monthly life annuity. If, at the member's death, payments

made have not exceeded the sum of the member's contributions plus interest as of the date of retirement, the balance is paid in a lump sum to the member's beneficiary. The 50% and 100% Survivor Options also are permitted for disability retirement. (A refund of the member's contribution account is paid for work-related disability.)

VIRGINIA SICKNESS AND DISABILITY PROGRAM (VSDP)

In lieu of disability retirement benefits, VRS state employees and VaLORS and SPORS members who elected this benefit (which is automatic for any new employee since January 1, 1999) are covered by the Virginia Sickness and Disability Program. These members will receive a deferred service retirement benefit payable at age 65 (age 60 for SPORS and VaLORS). The deferred benefit will be computed like a normal retirement benefit. For this calculation, a member's creditable service will include the period of disability, and the AFC will be adjusted to reflect increases in the cost of living between the date of disability and age 65. If the member dies while disabled, a death benefit will be determined as though the employee were an active member.

Deferred Retirement Benefit

ELIGIBILITY

A member with at least five years of service who does not withdraw his or her contributions from the fund is eligible for a deferred retirement benefit.

ANNUAL BENEFIT

The annual benefit is the same as the normal retirement benefit, but both AFC and service are determined at the time the member leaves active employment. Reduced benefits may commence at or after age 55 with at least five years of service, or at age 50 with 10 years of service (age 50 with at least five years of service for members of SPORS and VaLORS and employees of political subdivisions in hazardous duty positions receiving enhanced benefits).

PAYMENT FORM

The form of payment is the same as for Normal Retirement.

DEATH BENEFIT

The beneficiary of a member who dies after leaving active service but before retiring is entitled to receive a lump-sum distribution of the deceased member's contribution account.

Withdrawal (Refund) Benefit**ELIGIBILITY**

All members leaving covered employment are eligible. Vested members (those with five or more years of service) may withdraw their contributions plus interest instead of receiving the deferred retirement benefits otherwise due.

BENEFIT

A member who takes a refund receives a lump-sum payment of his or her member contributions, plus the interest credited on these contributions. Interest is credited at 4%, compounded annually on contributions in the account for at least one year.

Death Benefit**ELIGIBILITY**

Death must have occurred while a member is active or inactive and not retired.

BENEFIT

Upon the death of a non-vested active or inactive member, a refund of the member's contributions and interest is paid to the beneficiary. Upon the death of a vested active member, if the named beneficiary is the spouse, minor child or parent of the member, the beneficiary is eligible to receive a monthly benefit under the 100% Survivor Option. If death occurs before age 55 (age 50 for members of SPORS and VaLORS and employees of political subdivisions in hazardous duty positions receiving enhanced benefits), the member is assumed to be age 55 (age 50 for members of SPORS and VaLORS and employees of political subdivisions in hazardous duty positions receiving enhanced benefits) for benefit calculation purposes. A beneficiary may elect to receive a refund of the member's contributions plus interest in lieu of the monthly benefit.

WORK-RELATED DEATH

If the member's death is work-related, the surviving spouse, minor child or parent is eligible to receive 50% of

AFC if the survivor does not qualify for Social Security survivor benefits, or 33 1/3% of AFC if the survivor qualifies for Social Security survivor benefits. This benefit is reduced by Worker's Compensation. The named beneficiary receives a refund of the member's contributions and interest.

Optional Forms of Payment

Optional forms of payment are available on an actuarially equivalent basis, as follows:

100% SURVIVOR OPTION

This option is payable for the member's life. Upon the member's death, 100% of the benefit continues to the contingent annuitant.

VARIABLE SURVIVOR OPTION

For the member, the benefit is more than the 100% survivor option. Upon the member's death, a designated percentage of the benefit continues to the contingent annuitant.

ADVANCE PENSION OPTION

Allows an advance on future benefits. The member receives the higher payments in the early years of retirement and smaller payments (on an actuarially equivalent basis) at a future date the member specifies.

PARTIAL LUMP-SUM OPTION

This option allows the member with earned service beyond the normal retirement date to elect a lump-sum payment equal to the sum of 12, 24 or 36 payments of the standard monthly life annuity. The member's monthly benefit will be actuarially reduced to reflect the lump-sum payment. The member may then elect to receive the reduced monthly annuity under any of the other optional forms of payment.

COST-OF-LIVING ADJUSTMENTS

Members qualify for cost-of-living adjustments (COLAs) on July 1 of the second calendar year after retirement. Automatic COLAs are calculated as the first 3.0% of the Consumer Price Index increase plus half of each percentage increase from 3.0% to 7.0%. COLAs are capped at 5.0%.

Summary of Plan Changes

1996 Valuation

1. Any member with at least 25 years of service may purchase up to three years of prior service credit for (a) active duty military service in the armed forces of the United States; (b) certified creditable service in the retirement system of another state; or (c) both at the rate of 5% of current compensation or average final compensation if greater, times years of service purchased.
2. VRS may enter into an agreement with any political subdivision of the Commonwealth of Virginia that has a defined benefit plan that is not supplemental to VRS to permit portability of service credit on a cost-neutral basis.
3. Early retirement is allowed at age 50 with 10 years of service. The early retirement benefit is determined as if the member is age 55 (but using actual service and AFC), reduced by 0.6% for each month the member is younger than age 55. This benefit can be no smaller than the value of the member's contributions and interest paid in monthly installments over the member's lifetime.
4. The service multiplier for judges entering the Judicial Retirement System after January 1, 1995 is 2.5%.
5. Effective July 1, 1998, a health insurance credit of \$1.50 per month per year of service (up to 30 years) is provided to covered teachers who retire with at least 15 years of service. At local option, an additional credit of \$1 per month per year of service (up to 30 years) can be provided.

1998 Valuation

1. Effective January 1, 1999, the retirement benefit became 1.7% of AFC times years of service. The 3% benefit adjustment was eliminated for future retirees. A 2% ad hoc benefit increase was provided for all retirees and beneficiaries receiving benefits as of December 31, 1998.
2. The Virginia Sickness and Disability Program (VSDP) went into effect on January 1, 1999. New members since that date are automatically covered by this program and thus will only receive a deferred retirement benefit from VRS. Members joining before 1999 were allowed to make a one-time irrevocable election to join this program. (Applied to state employees and state police officers.)
3. Effective July 1, 1999, state employees, teachers and employees of participating political subdivisions that had not elected out of this benefit may retire with an unreduced benefit if they are at least age 50 and have earned at least 30 years of service.

1999 Valuation

1. 100% Joint and Survivor Option is payable in the case of a death of a member who dies while in active service.
2. 100% Joint and Survivor Option is payable for disability retirement.

2000 Valuation

1. The Virginia Law Officers' Retirement System went into effect on October 1, 1999.
2. On November 15, 2000, the VRS Board of Trustees adopted the recommended economic and demographic assumptions proposed by the actuary as a result of the June 2000 actuarial experience study.
3. The Board of Trustees adopted the use of a "pooled" contribution rate for state employees and teachers.

2001 Valuation

1. Members of SPORS had their temporary supplement starting at retirement extended from age 65 to their Social Security retirement age.
2. Members of VaLORS had their benefit multiplier changed from 1.7% to 2.0% of average final compensation with no temporary supplement for all new hires and rehires after July 1, 2001 as well as for current participants who made an election to change formulas.
3. The Partial Lump Sum Option was added as an optional form of payment. This option provides the retiring member with a lump-sum payment equal to the sum of either 12, 24 or 36 payments of the standard monthly life annuity. The member's monthly annuity is actuarially reduced to reflect the lump-sum payment.

2002 Valuation

No actuarially material changes were made in the plan provisions.

2003 Valuation

No actuarially material changes were made in the plan provisions. Listed below are two minor changes of note:

1. School superintendents with five years of service can purchase an additional 10 years of out-of-state service. The superintendent must not be eligible for an out-of-state benefit.
2. The leveling option was restored as an optional form of payment. Benefits may be leveled to age 62 or older, and the benefits cannot reduce more than 50%. Any COLAs are calculated on the basic benefit amount.

2004 Valuation

No actuarially material changes were made in the plan provisions.

2005 Valuation

1. No actuarially material changes were made in the plan provisions.
2. On May 19, 2005, the VRS Board of Trustees adopted the recommended economic and demographic assumptions proposed by the actuary as a result of the June 2004 actuarial experience study.

2006 Valuation

No actuarially material changes were made in the plan provisions.

Statistical Section

Pension Trust Funds:

- Analysis of Changes and Growth in Plan Net Assets
- Pension Trust Funds Additions Versus Deductions
- Number of Active Members
- Schedule of Retirement Contributions by System
- Pension Trust Funds Additions by Source
- Number of Retirees and Beneficiaries
- Retirement Benefits Paid
- Pension Trust Funds Deductions by Type
- Schedule of Retirement Benefits by System
- Schedule of Retirement Benefits by Type
- Schedule of Refunds by Type
- Schedule of Retirees and Beneficiaries by Type of Benefit and Option Selected
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Participating Employers

Program with Oversight by VRS – Deferred Compensation Plan of the Commonwealth of Virginia:

- Statement of Changes in Accumulation Plan Assets
- Operational Overview
- Deferred Compensation Plan Assets
- Contributions to the Deferred Compensation Plan
- Distributions from the Deferred Compensation Plan
- New Enrollments in the Deferred Compensation Plan
- Active and Inactive Deferred Compensation Plan Participants
- Total Participant Accounts in Each Fund Option
- Accumulation Plan Assets
- Description of Funds
- Investment Option Performance Summary



...at the right time...

One of the goals of VRS' long-range modernization program is to provide customers near 24/7 access to services and information. VRS staff made major strides toward this goal during the fiscal year:

- By June 30, 2007, more than 45,000 members had registered their secure online accounts through *myVRS*. During the year, members logged more than 80,000 visits to view their service, contributions and other VRS information. They also created nearly 83,000 retirement benefit estimates.
- VRS staff achieved key "early wins" toward the modernization program during the fiscal year. These included enhancements to the Retirement Information Management System.
- Staff also completed a major business process reengineering effort and identified essential business requirements in support of the next phases of modernization. These efforts defined the objectives and scope of this multi-year program and identified what new systems must do to enhance customer services in the future.

Pension Trust Funds

Analysis of Changes and Growth in Plan Net Assets

FOR THE YEARS ENDED JUNE 30

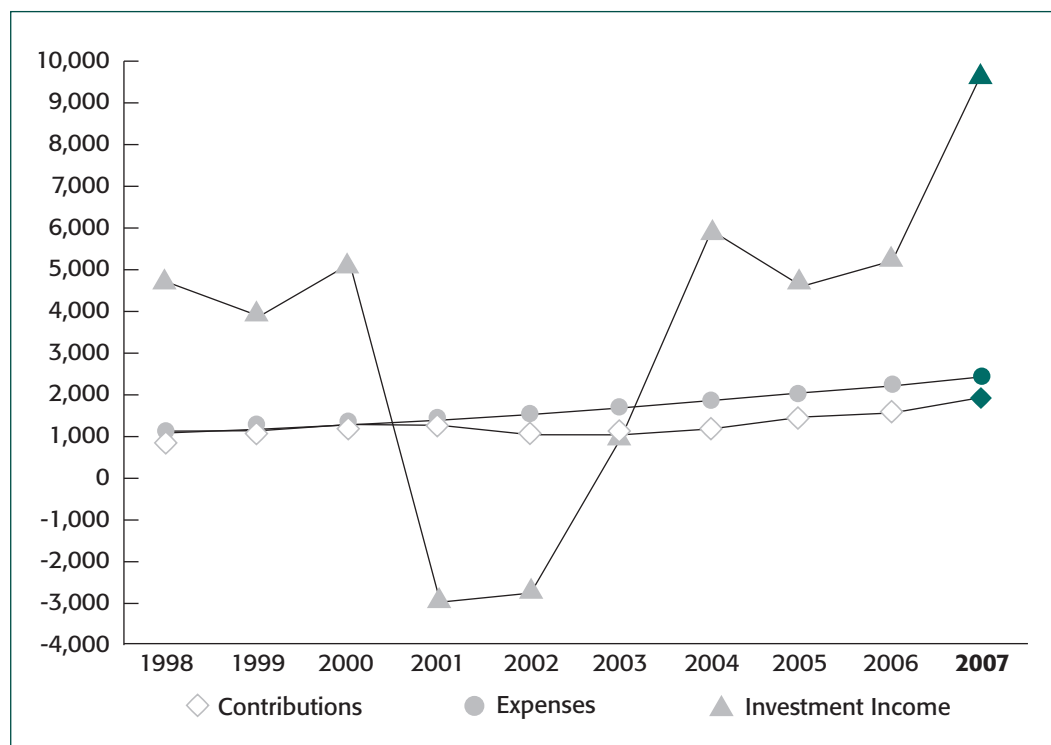
(EXPRESSED IN MILLIONS)

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Net Assets Available										
Beginning of Year	\$ 26,057	\$ 30,784	\$ 34,634	\$ 39,786	\$ 36,693	\$ 33,456	\$ 33,781	\$ 39,039	\$ 43,060	\$ 47,627
Member and Employer Contributions	1,131	1,141	1,291	1,270	1,044	1,042	1,185	1,468	1,567	1,944
Benefit and Administration Expenses	(1,090)	(1,176)	(1,282)	(1,394)	(1,529)	(1,687)	(1,865)	(2,049)	(2,214)	(2,434)
Net Funding	41	(35)	9	(124)	(485)	(645)	(680)	(581)	(647)	(490)
Investment Income										
Interest, Dividends and Other Investment Income	534	551	705	785	624	569	461	667	823	1,157
Net Appreciation (Depreciation) in Fair Value	4,152	3,334	4,438	(3,754)	(3,376)	401	5,477	3,935	4,391	8,596
Net Investment Income	4,686	3,885	5,143	(2,969)	(2,752)	970	5,938	4,602	5,214	9,753
Net Increase (Decrease)	4,727	3,850	5,152	(3,093)	(3,237)	325	5,258	4,021	4,567	9,263
Net Assets Available										
End of Year	\$ 30,784	\$ 34,634	\$ 39,786	\$ 36,693	\$ 33,456	\$ 33,781	\$ 39,039	\$ 43,060	\$ 47,627	\$ 56,890

Pension Trust Funds Additions Versus Deductions

FISCAL YEARS 1998-2007

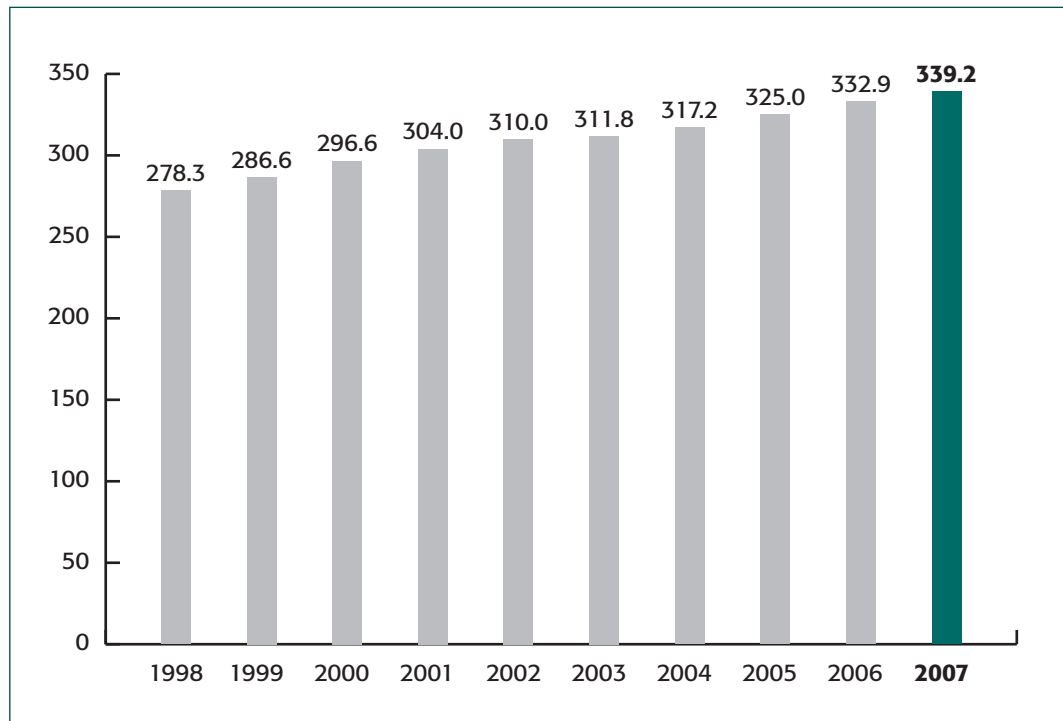
(MILLIONS OF DOLLARS)



Number of Active Members

FISCAL YEARS 1998-2007

(EXPRESSED IN THOUSANDS)



Schedule of Retirement Contributions by System

FISCAL YEARS 1998-2007

(EXPRESSED IN THOUSANDS)

Year Ended June 30	Virginia Retirement System				State Police Officers' Retirement System	Virginia Law Officers' Retirement System*	Judicial Retirement System	Total
	State	Teacher	Political	Sub-Total				
2007	\$ 377,117	\$ 945,243	\$ 511,687	\$1,834,047	\$ 21,466	\$ 64,820	\$ 23,437	\$1,943,770
2006	303,183	731,929	423,724	1,458,836	20,188	68,688	18,967	1,566,679
2005	295,736	671,152	398,004	1,364,892	19,363	66,079	17,927	1,468,261
2004	292,895	515,750	287,228	1,095,873	15,232	56,292	17,758	1,185,155
2003**	199,217	492,562	270,280	962,059	13,305	50,433	16,038	1,041,835
2002**	234,992	455,488	283,756	974,236	14,974	42,148	13,100	1,044,458
2001	299,079	591,620	264,229	1,154,928	24,632	67,040	23,149	1,269,749
2000	314,044	631,344	284,641	1,230,029	19,170	25,192	17,131	1,291,522
1999	296,748	556,712	257,140	1,110,600	15,298	-	15,034	1,140,932
1998	265,364	603,579	237,736	1,106,679	11,767	-	13,107	1,131,553

* The Virginia Law Officers' Retirement System went into effect on October 1, 1999.

** The Virginia General Assembly suspended employer contributions for all state employees effective January 2002. Employer contributions for SPORS, VaLORS, and JRS were resumed in July 2002 and for state employees in July 2003.

Pension Trust Funds Additions by Source

FISCAL YEARS 1998-2007

(EXPRESSED IN THOUSANDS)

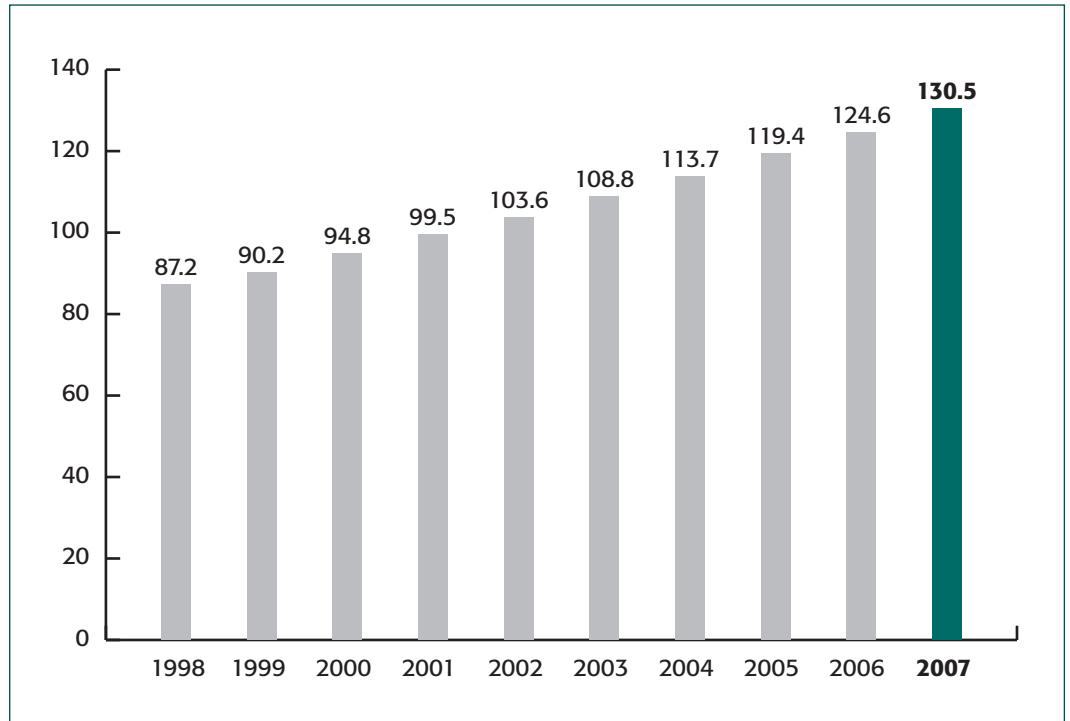
Year Ended June 30	Member Contributions	Employer Contributions		Investment Income (Loss)	Other	Total
		For Members	Employer Share			
VIRGINIA RETIREMENT SYSTEM (VRS)						
2007	\$ 29,489	\$ 680,023	\$ 1,124,535	\$ 9,426,035	\$ 338	\$ 11,260,420
2006	38,825	638,242	781,769	5,042,575	185	6,501,596
2005	63,503	599,769	701,620	4,453,335	743	5,818,970
2004	85,769	564,020	446,084	5,751,277	908	6,848,058
2003	127,578	499,077	335,404	935,415	2,682	1,900,156
2002	115,979	482,516	375,741	(2,667,982)	286	(1,693,460)
2001	65,810	453,133	635,985	(2,907,769)	381	(1,752,460)
2000	68,208	426,088	735,733	5,042,490	269	6,272,788
1999	55,710	406,543	648,347	3,809,905	703	4,921,208
1998	57,032	379,953	669,694	4,594,358	116	5,701,153
STATE POLICE OFFICERS' RETIREMENT SYSTEM (SPORS)						
2007	\$ 213	\$ 4,895	\$ 16,358	\$ 117,501	\$ -	\$ 138,967
2006	304	4,627	15,257	63,475	-	83,663
2005	494	4,392	14,477	56,481	-	75,844
2004	790	4,037	10,405	73,977	-	89,209
2003	556	3,972	8,777	11,929	-	25,234
2002	755	4,039	10,180	(34,596)	-	(19,622)
2001	125	4,087	20,420	(37,192)	-	(12,560)
2000	192	3,922	15,056	63,638	-	82,808
1999	179	3,548	11,571	47,974	-	63,272
1998	121	3,152	8,494	58,661	2	70,430
VIRGINIA LAW OFFICERS' RETIREMENT SYSTEM (VaLORS)						
2007	\$ 371	\$ 16,127	\$ 48,322	\$ 143,664	\$ 171	\$ 208,655
2006	534	15,492	52,662	71,905	255	140,848
2005	700	14,869	50,510	59,525	230	125,834
2004	880	14,703	40,709	70,668	-	126,960
2003	927	14,559	34,947	13,069	-	63,502
2002	1,007	15,630	25,511	(31,330)	-	10,818
2001	77	15,858	51,105	(4,057)	-	62,983
2000*	33	11,405	13,754	690	-	25,882
JUDICIAL RETIREMENT SYSTEM (JRS)						
2007	\$ 92	\$ 2,815	\$ 20,530	\$ 65,964	\$ -	\$ 89,401
2006	108	2,653	16,206	35,368	-	54,335
2005	159	2,499	15,269	31,379	-	49,306
2004	197	2,371	15,190	40,947	-	58,705
2003	88	2,346	13,604	6,543	-	22,581
2002	73	2,365	10,662	(19,248)	-	(6,148)
2001	4	2,315	20,830	(20,637)	-	2,512
2000	16	2,180	14,935	35,297	-	52,428
1999	6	2,049	12,979	26,569	-	41,603
1998	49	1,892	11,166	32,637	-	45,744

* The Virginia Law Officers' Retirement System went into effect on October 1, 1999.

Number of Retirees and Beneficiaries

FISCAL YEARS 1998-2007

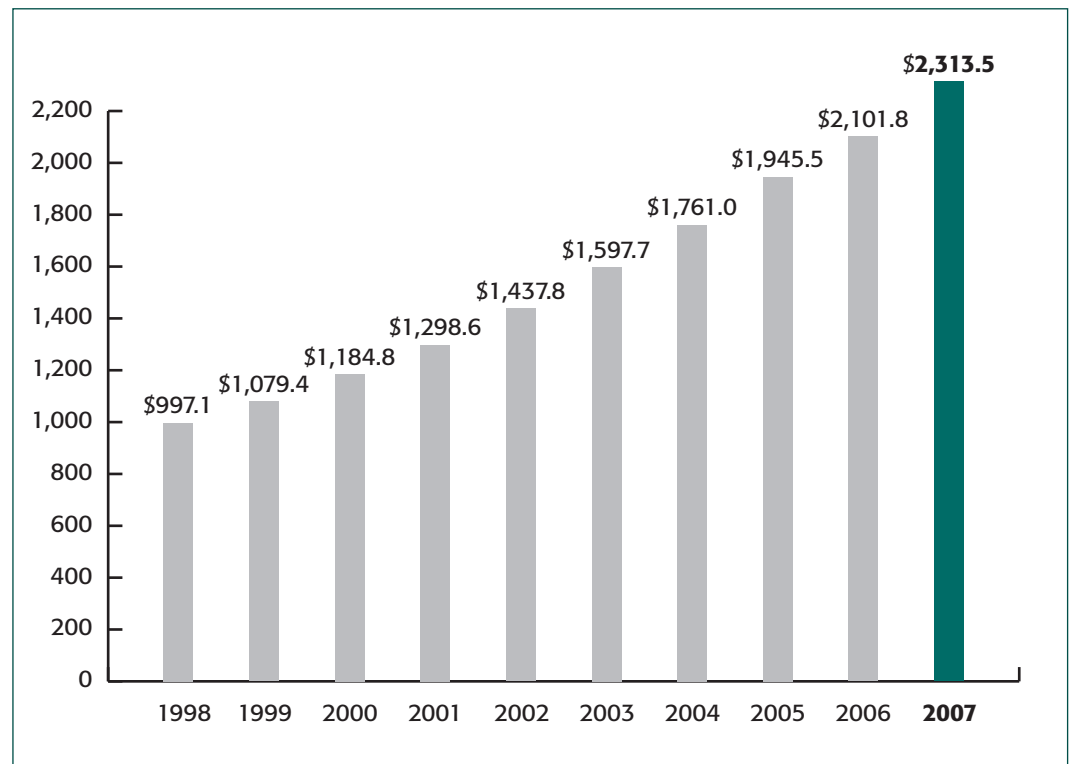
(EXPRESSED IN THOUSANDS)



Retirement Benefits Paid

FISCAL YEARS 1998-2007

(MILLIONS OF DOLLARS)



Pension Trust Funds Deductions by Type

FISCAL YEARS 1998-2007

(EXPRESSED IN THOUSANDS)

Year Ended June 30	Retirement Benefits	Refunds	Administrative Expenses	Other	Total
VIRGINIA RETIREMENT SYSTEM (VRS)					
2007	\$ 2,219,350	\$ 89,716	\$ 23,686	\$ 178	\$ 2,332,930
2006	2,015,557	85,804	19,724	258	2,121,343
2005	1,865,776	78,709	18,182	230	1,962,897
2004	1,692,166	80,237	18,119	–	1,790,522
2003	1,537,762	67,473	16,201	–	1,621,436
2002	1,389,815	69,235	15,039	2,449	1,476,538
2001	1,261,348	79,439	14,100	–	1,354,887
2000	1,150,694	83,412	12,613	–	1,246,719
1999	1,047,362	84,797	11,359	–	1,143,518
1998	966,876	81,168	10,980	123	1,059,147
STATE POLICE OFFICERS' RETIREMENT SYSTEM (SPORS)					
2007	\$ 33,867	\$ 1,221	\$ 301	\$ –	\$ 35,389
2006	32,309	596	231	–	33,136
2005	30,487	1,053	203	–	31,743
2004	26,336	731	213	–	27,280
2003	23,594	863	205	–	24,662
2002	20,607	559	185	–	21,351
2001	17,980	289	170	–	18,439
2000	16,946	314	137	–	17,397
1999	16,020	420	141	–	16,581
1998	15,324	474	139	–	15,937
VIRGINIA LAW OFFICERS' RETIREMENT SYSTEM (VaLORS)					
2007	\$ 35,019	\$ 4,828	\$ 365	\$ –	\$ 40,212
2006	29,202	4,830	263	–	34,295
2005	25,100	4,927	208	–	30,235
2004	19,784	3,998	196	–	23,978
2003	15,020	3,763	151	–	18,934
2002	8,485	3,657	57	–	12,199
2001	1,511	862	17	–	2,390
2000*	330	149	2	–	481
JUDICIAL RETIREMENT SYSTEM (JRS)					
2007	\$ 25,253	\$ –	\$ 169	\$ –	\$ 25,422
2006	24,717	–	130	–	24,847
2005	24,108	42	113	–	24,263
2004	22,706	–	117	–	22,823
2003	21,359	51	113	–	21,523
2002	18,884	–	104	–	18,988
2001	17,788	32	94	–	17,914
2000	16,872	24	105	–	17,001
1999	16,050	6	79	–	16,135
1998	14,856	–	78	–	14,934

* The Virginia Law Officers' Retirement System went into effect on October 1, 1999.

Schedule of Retirement Benefits by System

FISCAL YEARS 1998-2007

(EXPRESSED IN THOUSANDS)

Year Ended June 30	Virginia Retirement System				State Police Officers' Retirement System	Virginia Law Officers' Retirement System	Judicial Retirement System	Total
	State	Teacher	Political Subdivisions	Sub-Total				
2007	\$ 686,258	\$ 1,138,980	\$ 394,112	\$ 2,219,350	\$ 33,867	\$ 35,019	\$ 25,253	\$ 2,313,489
2006	623,571	1,037,509	354,477	2,015,557	32,309	29,202	24,717	2,101,785
2005	589,113	959,268	317,395	1,865,776	30,487	25,100	24,108	1,945,471
2004	552,282	855,113	284,771	1,692,166	26,336	19,784	22,706	1,760,992
2003	503,249	782,652	251,861	1,537,762	23,594	15,020	21,359	1,597,735
2002	454,123	710,538	225,154	1,389,815	20,607	8,485	18,884	1,437,791
2001	421,033	639,760	200,555	1,261,348	17,980	1,511	17,788	1,298,627
2000	394,601	575,876	180,217	1,150,694	16,946	330*	16,872	1,184,842
1999	372,503	514,124	160,735	1,047,362	16,020	–	16,050	1,079,432
1998	354,862	467,367	144,647	966,876	15,324	–	14,856	997,056

* The Virginia Law Officers' Retirement System went into effect on October 1, 1999.

Schedule of Retirement Benefits by Type

FISCAL YEARS 1998-2007

(EXPRESSED IN THOUSANDS)

Year Ended June 30	Service Benefits	Disability Benefits	Survivor Benefits	Total
2007	\$ 2,045,400	\$ 250,212	\$ 17,877	\$ 2,313,489
2006	1,849,239	236,266	16,280	2,101,785
2005	1,708,147	222,632	14,692	1,945,471
2004	1,537,173	210,385	13,434	1,760,992
2003	1,386,236	199,391	12,108	1,597,735
2002	1,242,235	184,582	10,974	1,437,791
2001	1,121,588	167,931	9,108	1,298,627
2000	1,021,185	155,450	8,207	1,184,842
1999	928,862	143,181	7,389	1,079,432
1998	861,377	128,637	7,042	997,056

Schedule of Refunds by Type

FISCAL YEARS 1998-2007

(EXPRESSED IN THOUSANDS)

Year Ended June 30	Separation	Death	Total
2007	\$ 88,661	\$ 7,104	\$ 95,765
2006	79,744	11,486	91,230
2005	76,296	8,435	84,731
2004	73,715	11,251	84,966
2003	64,203	7,947	72,150
2002	65,893	7,558	73,451
2001	73,659	6,963	80,622
2000	77,027	6,872	83,899
1999	78,530	6,693	85,223
1998	74,731	6,911	81,642

Schedule of Retirees and Beneficiaries by Type of Benefit and Option Selected

AS OF JUNE 30, 2007

Amount of Retirement Benefit	Number of Retirees	Service	Type of Retirement							
			Early Retirement Window	50/30 Service Retirement	1991 Fac. Early Retirement Window	Regular Disability	Survivor Payment-Death in Service	Line-of-Duty Disability	Survivor Payment-Death in Line-of-Duty	50/10 Provision
\$ 1 - 200	15,468	13,390	6	-	1	870	542	67	4	588
201 - 400	18,772	14,726	180	-	-	2,358	423	127	15	943
401 - 600	15,511	11,451	414	9	1	2,610	243	240	25	518
601 - 800	12,674	8,987	529	27	2	2,226	168	373	21	341
801 - 1,000	10,563	7,288	676	95	5	1,681	104	405	10	299
1,001 - 1,200	8,711	5,942	648	252	5	1,263	76	286	12	227
1,201 - 1,400	7,227	4,907	588	317	17	936	48	222	7	185
1,401 - 1,600	6,530	4,439	537	414	21	686	44	204	5	180
1,601 - 1,800	6,092	4,159	393	686	35	497	28	145	2	147
1,801 - 2,000	6,499	4,363	298	1,076	35	454	30	149	-	94
Over 2,001	22,453	16,335	588	3,619	156	1,023	96	409	2	225
Totals	130,500	95,987	4,857	6,495	278	14,604	1,802	2,627	103	3,747

Min. Guar. Amount of Retirement Benefit	Option Selected															
	A	B	C	D	E	F	H	K	L	M	N	R	V	X	Y	Z
\$ 1 - 200	12,608	67	529	187	1,054	2	80	4	-	3	711	8	176	11	22	6
201 - 400	14,713	30	580	360	977	7	883	32	2	23	695	3	374	41	42	10
401 - 600	11,371	33	483	422	945	14	1,203	64	-	54	509	1	304	42	58	8
601 - 800	8,893	22	417	459	903	11	983	58	-	76	393	4	328	35	80	12
801 - 1,000	7,200	8	355	499	875	19	636	39	1	29	347	1	357	42	135	20
1,001 - 1,200	5,770	2	327	461	741	12	413	28	1	26	231	4	401	46	203	45
1,201 - 1,400	4,815	3	273	410	492	22	253	20	1	12	167	5	383	61	244	66
1,401 - 1,600	4,348	1	261	381	342	33	157	6	-	10	150	1	378	66	315	81
1,601 - 1,800	4,144	-	206	349	200	34	83	5	-	3	109	2	360	61	432	104
1,801 - 2,000	4,422	-	165	343	139	31	69	5	-	3	114	4	352	73	651	128
Over 2,001	13,414	1	543	1,023	223	190	82	11	-	5	473	54	2,136	576	3,064	658
Totals	91,698	167	4,139	4,894	6,891	375	4,842	272	5	244	3,899	87	5,549	1,054	5,246	1,138

- A = Basic Benefit
- B = Increased Basic Benefit
- C = 100% Survivor Benefit
- D = 50% Survivor Benefit
- E = Social Security Leveling Benefit
- F = Special Survivor Option
- H = Minimum Guaranteed Disability Basic Benefit
- K = Minimum Guaranteed Disability -50% Survivor
- L = 100% Survivor - Disability
- M = Special Survivor Option - Disability
- N = Leveling Benefit
- R = Leveling Benefit - Rollover
- V = Survivor Option
- X = Advance Pension Option
- Y = PLOP Basic
- Z = PLOP with Survivor

Retirement breakdown: During FY 2007, 90% of all retirements were service retirements, and 10% were certified as disability retirements by the Medical Board.

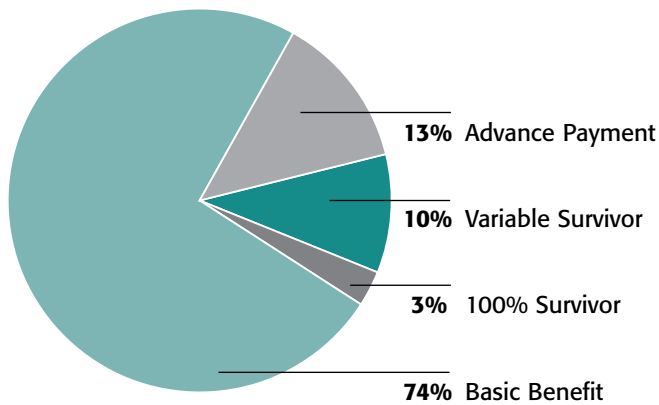
Schedule of Average Benefit Payments

RETIREMENT EFFECTIVE DATE JULY 1, 2002 TO JUNE 30, 2007

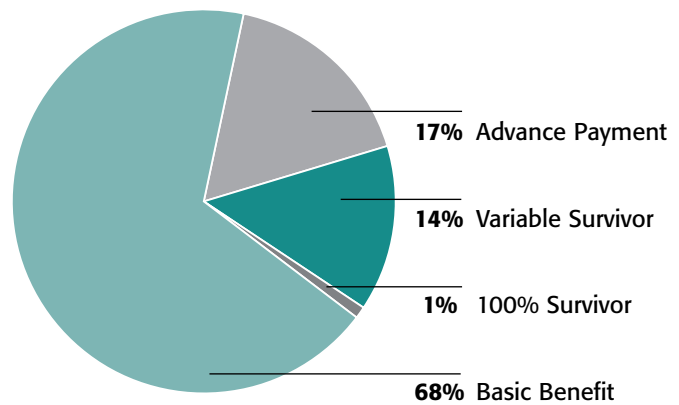
		Years of Credited Service					
		1-10	11-15	16-20	21-25	26-30	Over 30
FY 2007	Average Monthly Benefit	\$ 314.54	\$ 509.88	\$ 811.90	\$ 1,159.16	\$ 1,917.95	\$ 2,474.52
	Number of Active Retirees	979	880	951	1,043	1,504	3,207
FY 2006	Average Monthly Benefit	\$ 306.43	\$ 496.82	\$ 775.31	\$ 1,131.49	\$ 1,811.18	\$ 2,438.66
	Number of Active Retirees	890	809	960	937	1,569	2,886
FY 2005	Average Monthly Benefit	\$ 316.96	\$ 496.99	\$ 745.37	\$ 1,066.32	\$ 1,773.77	\$ 2,352.01
	Number of Active Retirees	768	784	902	921	1,623	3,342
FY 2004	Average Monthly Benefit	\$ 311.29	\$ 492.98	\$ 716.50	\$ 1,057.30	\$ 1,726.91	\$ 2,396.00
	Number of Active Retirees	694	711	867	851	1,582	2,935
FY 2003	Average Monthly Benefit	\$ 326.30	\$ 473.50	\$ 686.13	\$ 1,052.83	\$ 1,739.64	\$ 2,389.74
	Number of Active Retirees	659	794	798	958	1,575	2,904

Distribution of Retirees by Payment Option Selected

ALL RETIREES AT JUNE 30, 2007



2007 RETIREES



Retirement Options

Basic Benefit

Monthly annuity payments are based on the normal benefit formula. Any accumulated contributions that have not been used between the date of retirement and the date of death are paid in a lump sum to the designated beneficiaries.

Variable Survivor

For the retiree, the benefit is more than the 100% survivor option benefit. At death, a percentage of the monthly benefit is continued to the designated contingent annuitant.

100% Survivor

The basic benefit is reduced during the member's lifetime. At death, the benefit is continued in the same amount to the designated contingent annuitant.

Advance Payment

LEVELING/SOCIAL SECURITY

As an advance on the benefit, the retiree receives a higher benefit in the early years of retirement. The advance is paid from the retirement date until the age specified by the retiree (between 59½ and 70½, or age 65 under the Social Security option). This benefit reduces at the leveling age.

PARTIAL LUMP SUM

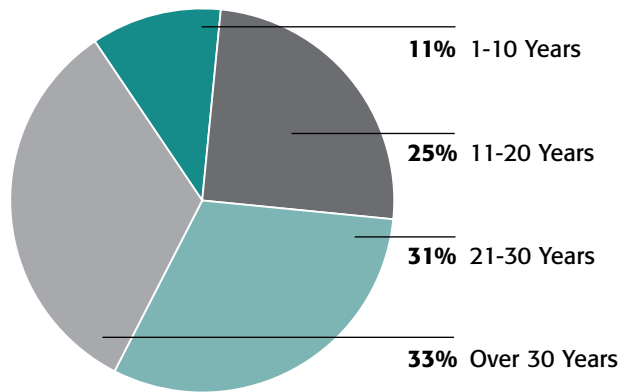
This option allows members with earned service beyond their normal retirement date to elect a lump-sum payment equal to the sum of 12, 24 or 36 payments of the standard monthly life annuity. The member's monthly benefit will be actuarially reduced to reflect the lump-sum payment.



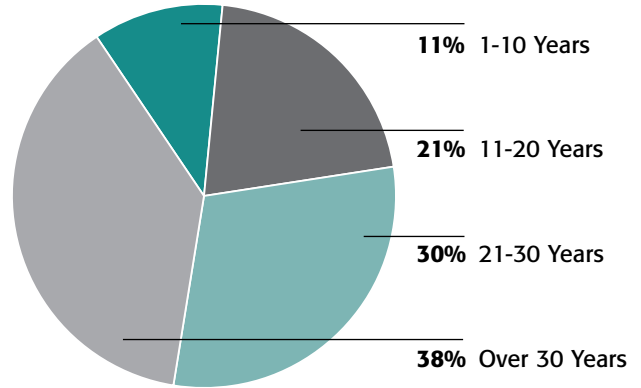
Retirees and beneficiaries increased 4.7%, from 124,639 in fiscal year 2006 to 130,500 in fiscal year 2007.

Distribution of Retirees by Years of Service

ALL RETIREES AT JUNE 30, 2007

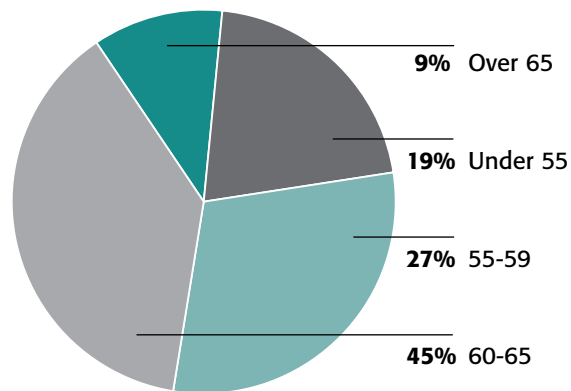


2007 RETIREES

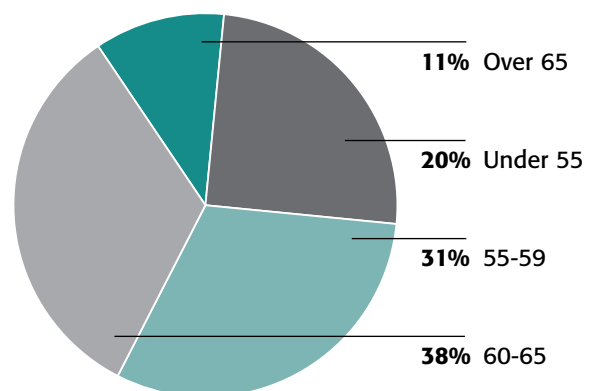


Distribution of Retirees by Age at Retirement

ALL RETIREES AT JUNE 30, 2007

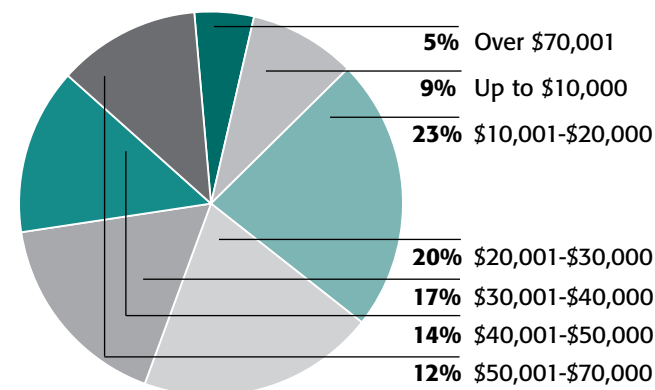


2007 RETIREES

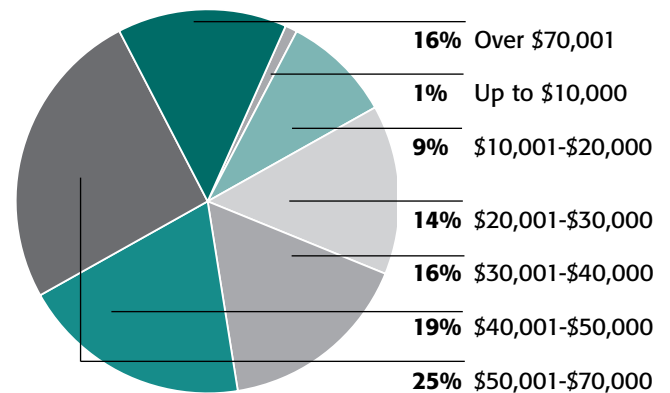


Distribution of Retirees by Average Final Compensation

ALL RETIREES AT JUNE 30, 2007



2007 RETIREES



Other Employee Benefit Trust Funds

Schedule of Group Insurance Fund Additions by Source

FISCAL YEARS 1998-2007

(EXPRESSED IN THOUSANDS)

Year Ended June 30	Contributions				Investment Income (Loss)	Other	Total
	State	Teacher	Political Subdivisions	Sub-Total			
2007	\$ 51,116	\$ 74,442	\$ 44,266	\$ 169,824	\$ 160,881	\$ -	\$ 330,705
2006*	(2)	-	54	52	92,187	-	92,239
2005*	1	(33)	1	(31)	91,547	-	91,516
2004*	1	-	19	20	133,715	-	133,735
2003*	5	22	17	44	18,297	-	18,341
2002*	22,919	28,267	17,614	68,800	(72,021)	-	(3,221)
2001	29,703	37,027	21,894	88,624	(77,363)	-	11,261
2000*	1	2	41	44	139,707	277	140,028
1999*	(1)	1	22	22	110,393	-	110,415
1998	8,973	10,958	6,435	26,366	145,280	-	171,646

* The group life insurance contribution rates for fiscal years 2006, 2005, 2004, 2003, 2000 and 1999 were zero. Amounts shown are adjustments and contributions for new employers. There was also a premium holiday beginning in April 2002.

Schedule of Group Insurance Fund Deductions by Type

FISCAL YEARS 1998-2007

(EXPRESSED IN THOUSANDS)

Year Ended June 30	Group Life Claims			Administrative Expenses	Other	Total
	Active	Retired	Sub-Total			
2007	\$ 46,322	\$ 72,305	\$ 118,627	\$ 568	\$ 543	\$ 119,738
2006	43,140	68,350	111,490	716	489	112,695
2005	37,139	59,902	97,041	678	444	98,163
2004	42,290	63,741	106,031	615	372	107,018
2003	44,614	59,661	104,275	644	276	105,195
2002	39,617	56,008	95,625	474	198	96,297
2001	36,899	51,280	88,179	475	170	88,824
2000	34,113	48,912	83,025	626	196	83,847
1999	23,309	36,772	60,081	912	220	61,213
1998	26,854	45,919	72,773	801	198	73,772

Schedule of Retiree Health Insurance Credit Fund Additions and Deductions

FISCAL YEARS 1998-2007

(EXPRESSED IN THOUSANDS)

Year Ended June 30	Additions				Deductions		
	Contributions	Investment Income (Loss)	Other	Total	Health Insurance Reimbursements	Administrative Expenses	Total
2007	\$ 92,919	\$ 34,422	\$ -	\$ 127,341	\$ 80,447	\$ 356	\$ 80,803
2006	86,913	17,018	-	103,931	72,482	337	72,819
2005	81,995	13,540	-	95,535	68,966	508	69,474
2004	78,383	15,582	-	93,965	64,920	372	65,292
2003	74,123	3,265	-	77,388	61,027	323	61,350
2002	85,209	(5,080)	-	80,129	57,590	335	57,925
2001	73,901	(3,089)	-	70,812	54,628	347	54,975
2000***	17,592	6,323	-	23,915	50,456	324	50,780
1999**	35,260	7,689	1	42,950	30,254	321	30,575
1998*	22,123	7,637	14	29,774	17,372	-	17,372

* There was no direct charge to the program for administration in FY 1998.

** Data for FY 1999 reflects extension of coverage to all teachers on July 1, 1998 and a premium holiday for state employees in May and June 1999.

*** No contributions were paid for state employees during FY 2000. The maximum health credit for state employees increased to \$120 per month and for teachers to \$75 per month effective July 1, 1999.

Schedule of Disability Insurance Trust Fund Additions and Deductions

FISCAL YEARS 1998-2007

(EXPRESSED IN THOUSANDS)

Year Ended June 30	Additions				Deductions		
	Contributions	Investment Income (Loss)	Other	Total	Disability Insurance Benefits	Administrative Expenses	Total
2007	\$ 65,726	\$ 40,036	\$ -	\$ 105,762	\$ 33,282	\$ 766	\$ 34,048
2006	57,991	17,562	-	75,553	27,339	576	27,915
2005	54,505	12,723	-	67,228	25,840	476	26,316
2004	35,247	14,198	-	49,445	23,835	671	24,506
2003	34,813	3,235	-	38,048	16,780	791	17,571
2002	27,850	(4,012)	-	23,838	11,578	491	12,069
2001	27,233	(2,918)	-	24,315	8,336	729	9,065
2000	25,317	2,480	-	27,797	4,647	678	5,325
1999*	10,091	353	-	10,444	1,273	756	2,029

* The Virginia Sickness and Disability Program went into effect on January 1, 1999.

Participating Employers

AS OF JUNE 30, 2007

Political

Subdivisions (432)

Accomack County
 Albemarle County
 Alleghany County
 Amelia County
 Amherst County
 Appomattox County
 Augusta County
 Bath County
 Bedford County
 Bland County
 Botetourt County
 Brunswick County
 Buchanan County
 Buckingham County
 Campbell County
 Caroline County
 Carroll County
 Charles City County
 Charlotte County
 Chesterfield County
 Clarke County
 Craig County
 Culpeper County
 Cumberland County
 Dickenson County
 Dinwiddie County
 Essex County
 Fauquier County
 Floyd County
 Fluvanna County
 Franklin County
 Frederick County
 Giles County
 Gloucester County
 Goochland County
 Grayson County
 Greene County
 Greensville County
 Halifax County
 Hanover County
 Henrico County
 Henry County
 Highland County
 Isle of Wight County
 James City County
 King & Queen County
 King George County
 King William County
 Lancaster County
 Lee County
 Loudoun County
 Louisa County
 Lunenburg County

Madison County
 Mathews County
 Mecklenburg County
 Middlesex County
 Montgomery County
 Nelson County
 New Kent County
 Northampton County
 Northumberland County
 Nottoway County
 Orange County
 Page County
 Patrick County
 Pittsylvania County
 Powhatan County
 Prince Edward County
 Prince George County
 Prince William County
 Pulaski County
 Rappahannock County
 Richmond County
 Roanoke County
 Rockbridge County
 Rockingham County
 Russell County
 Scott County
 Shenandoah County
 Smyth County
 Southampton County
 Spotsylvania County
 Stafford County
 Surry County
 Sussex County
 Tazewell County
 Warren County
 Washington County
 Westmoreland County
 Wise County
 Wythe County
 York County
 City of Alexandria
 City of Bedford
 City of Bristol
 City of Buena Vista
 City of Chesapeake
 City of Colonial Heights
 City of Covington
 City of Danville
 City of Emporia
 City of Fairfax
 City of Falls Church
 City of Franklin
 City of Fredericksburg
 City of Galax
 City of Hampton

City of Harrisonburg
 City of Hopewell
 City of Lexington
 City of Lynchburg
 City of Manassas
 City of Manassas Park
 City of Martinsville
 City of Norfolk
 City of Norton
 City of Petersburg
 City of Poquoson
 City of Portsmouth
 City of Radford
 City of Richmond
 City of Roanoke
 City of Salem
 City of Staunton
 City of Suffolk
 City of Virginia Beach
 City of Waynesboro
 City of Williamsburg
 City of Winchester
 Town of Abingdon
 Town of Alberta
 Town of Altavista
 Town of Amherst
 Town of Appomattox
 Town of Ashland
 Town of Berryville
 Town of Big Stone Gap
 Town of Blacksburg
 Town of Blackstone
 Town of Bluefield
 Town of Bowling Green
 Town of Boyce
 Town of Boydton
 Town of Boykins
 Town of Bridgewater
 Town of Broadway
 Town of Brodnax
 Town of Brookneal
 Town of Burkeville
 Town of Cape Charles
 Town of Chase City
 Town of Chatham
 Town of Chilhowie
 Town of Chincoteague
 Town of Christiansburg
 Town of Clarksville
 Town of Clifton Forge
 Town of Coeburn
 Town of Colonial Beach
 Town of Courtland
 Town of Craigsville
 Town of Crewe

Town of Culpeper
 Town of Dayton
 Town of Dillwyn
 Town of Dublin
 Town of Dumfries
 Town of Edinburg
 Town of Elkton
 Town of Exmore
 Town of Floyd
 Town of Front Royal
 Town of Gate City
 Town of Glasgow
 Town of Gordonsville
 Town of Gretna
 Town of Grottoes
 Town of Grundy
 Town of Halifax
 Town of Hamilton
 Town of Haysi
 Town of Herndon
 Town of Hillsville
 Town of Hurt
 Town of Independence
 Town of Iron Gate
 Town of Jarratt
 Town of Jonesville
 Town of Kenbridge
 Town of Kilmarnock
 Town of La Crosse
 Town of Lawrenceville
 Town of Leesburg
 Town of Louisa
 Town of Luray
 Town of Madison
 Town of Marion
 Town of Mckenney
 Town of Middleburg
 Town of Middletown
 Town of Montross
 Town of Mt. Jackson
 Town of Narrows
 Town of New Market
 Town of Onancock
 Town of Onley
 Town of Orange
 Town of Parksley
 Town of Pearisburg
 Town of Pembroke
 Town of Pennington Gap
 Town of Pound
 Town of Pulaski
 Town of Purcellville
 Town of Quantico
 Town of Remington
 Town of Rich Creek

Town of Rocky Mount	Blue Ridge Juvenile Detention Center	Evergreen Soil & Water Conservation District	Middle Peninsula-Northern Neck Community Services Board
Town of Round Hill	Blue Ridge Regional Jail Authority	Fauquier County Water & Sanitation Authority	Middle Peninsula Regional Security Center
Town of Rural Retreat	Bristol Redevelopment & Housing Authority	Ferrum Water & Sewage Authority	Middle River Regional Jail Authority
Town of Saltville	Brunswick Industrial Development Authority	Franklin Redevelopment & Housing Authority	Monacan Soil & Water Conservation District
Town of Scottsville	Campbell County Utilities & Service Authority	Frederick County Sanitation Authority	Montgomery Regional Solid Waste Authority
Town of Shenandoah	Capital Regional Airport Commission	Fredericksburg-Stafford Park Authority	Nelson County Service Authority
Town of Smithfield	Central Rappahannock Regional Library	Giles County Public Service Authority	New River Resource Authority
Town of South Boston	Central Virginia Community Services Board	Goochland-Powhatan Community Services Board	New River Soil & Water Conservation District
Town of South Hill	Central Virginia Regional Jail	Greensville County Water & Sewer Authority	New River Valley Community Services Board
Town of St. Paul	Central Virginia Waste Management Authority	Greensville-Emporia Department of Social Services	New River Valley Juvenile Detention Home Commission
Town of Stanley	Charles Pickney Jones Memorial Library	Hampton-Newport News Community Services Board	New River Valley Planning District Commission
Town of Stephens City	Charlottesville-Albemarle Airport Authority	Hampton Redevelopment & Housing Authority	New River Valley Regional Jail
Town of Strasburg	Charlottesville Redevelopment & Housing Authority	Hampton Roads Planning District Commission	Norfolk Airport Authority
Town of Stuart	Chesapeake Bay Bridge & Tunnel District	Hampton Roads Regional Jail Authority	Norfolk Redevelopment & Housing Authority
Town of Tappahannock	Chesapeake Redevelopment & Housing Authority	Hampton Roads Sanitation District	Northern Neck-Essex County Group Home Commission
Town of Tazewell	Chesterfield County Health Center Commission	Hampton Roads Transit	Northern Neck Planning District Commission
Town of Timberville	Clinch Valley Soil & Water Conservation District	Handley Library Board	Northern Neck Regional Jail
Town of Urbanna	Coeburn-Norton-Wise Regional Water Treatment Authority	Harrisonburg-Rockingham Community Services Board	Northern Shenandoah Valley Regional Commission
Town of Victoria	Colonial Services Board	Harrisonburg-Rockingham Regional Sewer Authority	Northern Virginia Health Care Center Commission
Town of Vienna	Colonial Soil & Water Conservation District	Henricopolis Soil & Water Conservation District	Northern Virginia Juvenile Detention Home
Town of Vinton	Commonwealth Regional Council	Henry County Public Service Authority	Northwestern Community Services Board
Town of Wakefield	Crater Juvenile Detention Home Commission	Holston River Soil & Water Conservation District	Opportunity Inc. of Hampton Roads
Town of Warrenton	Culpeper Soil & Water Conservation District	Hopewell Redevelopment & Housing Authority	Pamunkey Regional Jail
Town of Warsaw	Cumberland Mountain Community Services Board	Industrial Development Authority of Henrico County	Peaks of Otter Soil & Water Conservation District
Town of Waverly	Cumberland Plateau Regional Housing Authority	Institute for Advanced Learning and Research	Peninsula Airport Commission
Town of Weber City	Daniel Boone Soil & Water Conservation District	James City Service Authority	Pepper's Ferry Regional Wastewater Authority
Town of West Point	Danville-Pittsylvania Community Services Board	John Marshall Soil & Water Conservation District	Peter Francisco Soil & Water Conservation District
Town of Windsor	Danville Redevelopment & Housing Authority	Lee County Redevelopment & Housing Authority	Petersburg Redevelopment & Housing Authority
Town of Wise	Dinwiddie County Water Authority	Lee County Public Service Authority	Peumansend Creek Regional Jail
Town of Woodstock	District 19 Community Services Board	Lenwisco Planning District Commission	Piedmont Regional Jail
Town of Wytheville	Eastern Shore Community Services Board	Lonesome Pine Regional Library	Piedmont Regional Juvenile Detention Center
Accomack-Northampton Planning District Commission	Eastern Shore Public Library	Loudoun County Sanitation Authority	Pittsylvania County Service Authority
Albemarle County Service Authority	Eastern Shore Soil & Water Conservation District	Massanuttan Regional Library	Planning District One Behavioral Health Services Board
Albermarle-Charlottesville Regional Jail		Meherrin Regional Library	Potomac and Rappahannock Transportation Commission

Potomac River Fisheries Commission	Southside Planning District Commission	Public School Boards – Professional Employees	Campbell County Schools*
Prince William County Service Authority	Southside Regional Jail	<i>City/Town Schools (39)</i>	Caroline County Schools*
Prince William Soil & Water Conservation District	Southside Regional Juvenile Group Home Commission	Alexandria City Schools*	Carroll County Schools*
Rappahannock Area Community Services Board	Southside Regional Library Board	Bristol City Schools*	Charles City County Schools*
Rappahannock Juvenile Center	Southwest Virginia Regional Jail	Buena Vista City Schools*	Charlotte County Schools*
Rappahannock-Rapidan Community Services Board	Spotsylvania-Stafford-Fredericksburg Group Home Commission	Charlottesville Public Schools*	Chesterfield County Schools*
Rappahannock-Rapidan Regional Planning District Commission	Staunton Redevelopment & Housing Authority	Chesapeake Public Schools*	Clarke County Schools*
Rappahannock Regional Jail	Suffolk Redevelopment & Housing Authority	Colonial Beach Schools	Craig County Schools*
Region Ten Community Services Board	Sussex Service Authority	Colonial Heights City Schools*	Culpeper County Schools*
Richmond Metropolitan Authority	Tazewell Soil & Water Conservation District	Covington City Schools*	Cumberland County Schools*
Richmond Redevelopment & Housing Authority	Thomas Jefferson Planning District Commission	Danville City Schools*	Dickenson County Schools*
Richmond Regional Planning District Commission	Thomas Jefferson Soil & Water Conservation District	Fairfax City Schools	Dinwiddie County Schools*
Rivanna Solid Waste Authority	Tidewater Regional Group Home Commission	Falls Church Public Schools	Essex County Schools*
Rivanna Water & Sewer Authority	Tidewater Soil & Water Conservation District	Franklin City Schools*	Fairfax County Schools
Riverside Regional Jail	Tri-County/City Soil & Water Conservation District	Fredericksburg City Schools*	Fauquier County Schools*
Roanoke Higher Education Authority	Upper Occoquan Sewage Authority	Galax City Schools*	Floyd County Schools*
Roanoke River Service Authority	Valley Community Services Board	Hampton City Schools*	Fluvanna County Schools*
Robert E. Lee Soil & Water Conservation District	Virginia Biotechnology Research Park Authority	Harrisonburg City Schools*	Franklin County Schools*
Rockbridge Area Community Services Board	Virginia Coalfield Economic Development Authority	Hopewell City Schools*	Frederick County Schools*
Rockbridge Area Social Services Department	Virginia Highlands Airport Commission	Lexington City Schools*	Giles County Schools*
Rockbridge County Public Service Authority	Virginia Peninsula Regional Jail	Lynchburg Public Schools*	Gloucester County Schools*
Rockbridge Regional Library	Virginia Peninsulas Public Service Authority	Manassas City Schools*	Goochland County Schools*
Russell County Water & Sewage Authority	Virginia Resources Authority	Manassas Park City Schools*	Grayson County Schools*
Scott County Public Service Authority	Washington County Service Authority	Martinsville City Schools*	Greene County Schools*
Scott County Redevelopment & Housing Authority	Waynesboro Redevelopment & Housing Authority	Newport News Public Schools	Greensville County Schools*
Scott County Soil & Water Conservation District	Western Tidewater Community Services Board	Norfolk Public Schools*	Halifax County Schools*
Shenandoah Valley Juvenile Detention Home Commission	Western Tidewater Regional Jail	Norton City Schools*	Hanover County Schools*
Shenandoah Valley Regional Airport Commission	Western Virginia Water Authority	Petersburg City Schools*	Henrico County Schools*
Skyline Soil & Water Conservation District	Wise County Public Service Authority	Poquoson City Schools*	Henry County Schools*
South Central Wastewater Authority	Wise County Redevelopment & Housing Authority	Portsmouth City Schools*	Highland County Schools*
Southeastern Virginia Public Services Authority	Wythe-Grayson Regional Library	Radford City Schools*	Isle of Wight County Schools*
Southside Community Services Board	Wytheville Redevelopment & Housing Authority	Richmond Public Schools*	King & Queen County Schools*
		Roanoke City Schools*	King George County Schools*
		Salem City Schools*	King William County Schools*
		Staunton City Schools*	Lancaster County Schools*
		Suffolk City Schools*	Lee County Schools*
		Virginia Beach City Schools*	Loudoun County Schools*
		Waynesboro City Schools*	Louisa County Schools*
		West Point Schools	Lunenburg County Schools*
		Williamsburg-James City County Schools*	Madison County Schools*
		Winchester Public Schools*	Mathews County Schools*
			Mecklenburg County Schools*
		<i>County Schools (94)</i>	Middlesex County Schools*
		Accomack County Schools*	Montgomery County Schools*
		Albemarle County Schools*	Nelson County Schools*
		Alleghany County Schools*	New Kent County Schools*
		Amelia County Schools*	Northampton County Schools*
		Amherst County Schools*	Northumberland County Schools*
		Appomattox County Schools*	Nottoway County Schools*
		Arlington County Schools*	Orange County Schools*
		Augusta County Schools*	Page County Schools*
		Bath County Schools*	Patrick County Schools*
		Bedford County Schools*	Pittsylvania County Schools*
		Bland County Schools*	Powhatan County Schools*
		Botetourt County Schools*	Prince Edward County Schools*
		Brunswick County Schools*	Prince George County Schools*
		Buchanan County Schools*	Prince William County Schools*
		Buckingham County Schools*	Pulaski County Schools*
			Rappahannock County Schools*

Richmond County Schools*	Warren County Schools*	Governor's School for	Rowanty Vocational
Roanoke County Schools*	Washington County Schools*	Global Economics and	Technical Center
Rockbridge County Schools*	Westmoreland County	Technology	The Pruden Center for
Rockingham County Schools*	Schools*	Jackson River Vocational	Industry and Technology*
Russell County Schools*	Wise County Schools*	Technical Center*	Valley Vocational Technical
Scott County Schools*	Wythe County Schools*	Maggie Walker Governor's	Center*
Shenandoah County Schools*	York County Schools*	School for Government and	
Smyth County Schools*	<i>Other Schools (12)</i>	International Studies	*Non-Professional employees
Southampton County Schools*	Amelia-Nottoway Vocational	New Horizons Technical	also covered (133 School
Spotsylvania County Schools*	Center	Center*	Boards)
Stafford County Schools*	Appomattox Regional	Northern Neck Regional	Agencies of the
Surry County Schools*	Governor's School*	Special Education Program	Commonwealth of Virginia
Sussex County Schools*	Charlottesville-Albemarle	Northern Neck Regional	(237)
Tazewell County Schools*	Vocational Technical Center	Vocational Center*	

VRS Employer Ranking at June 30, 2007

Employer	Active Employees	Rank	Percentage of Total
Fairfax County Schools - Professional Employees	19,297	1	5.69%
Virginia Beach City Schools - Professional Employees	8,496	2	2.51%
Prince William County Schools - Professional Employees	7,309	3	2.16%
Loudoun County Schools - Professional Employees	6,053	4	1.78%
Chesterfield County Schools - Professional Employees	5,983	5	1.76%
City of Virginia Beach	5,887	6	1.74%
University of Virginia - Academic Division	5,340	7	1.57%
Norfolk City Schools - Professional Employees	5,133	8	1.51%
Virginia Polytechnic Institute and State University	4,792	9	1.41%
Henrico County	4,711	10	1.39%
All other	266,214		78.48%
Total	339,215		100.00%

Program with Oversight by VRS

Deferred Compensation Plan of the Commonwealth of Virginia

The Deferred Compensation Plan is regulated by Chapter Six of Title 51.1 of the *Code of Virginia* and is intended to be an eligible plan within the meaning of Internal Revenue Code 457(b). The purpose of the plan is to provide participants with a convenient way to save for retirement through deferrals of compensation. The plan is available, on a voluntary basis, to all salaried and wage employees, including elected and appointed officials providing services to the Commonwealth as well as eligible employees of participating political subdivisions.

Statement of Changes in Accumulation Plan Assets

YEARS ENDED JUNE 30, 2007 AND 2006

	2007	2006
Plan Assets on July 1	\$ 864,272,511	\$ 728,544,490
Contributions	109,320,357	107,199,887
Distributions	(45,525,487)	(33,198,867)
Plan Transfers ¹	435,354	766,405
Third-Party Administration Fees ²	(2,394,850)	(2,175,759)
Period Earnings	129,317,052	63,136,355
Plan Assets on June 30	\$1,055,424,937	\$ 864,272,511

¹ Represents plan transfers from other eligible Section 457(b) plans into the Commonwealth's Plan.

² The current third-party administrator, Great-West Retirement Services, is compensated based on an annual recordkeeping and communication fee of 28 basis points (0.28%) capped at account balances of \$130,000. In addition, administrative costs were incurred by VRS in FY 2007 and FY 2006 of \$248,940 and \$198,263, respectively. These costs are funded by the employers participating in the plan.

Deferred Compensation Plan – Operational Overview

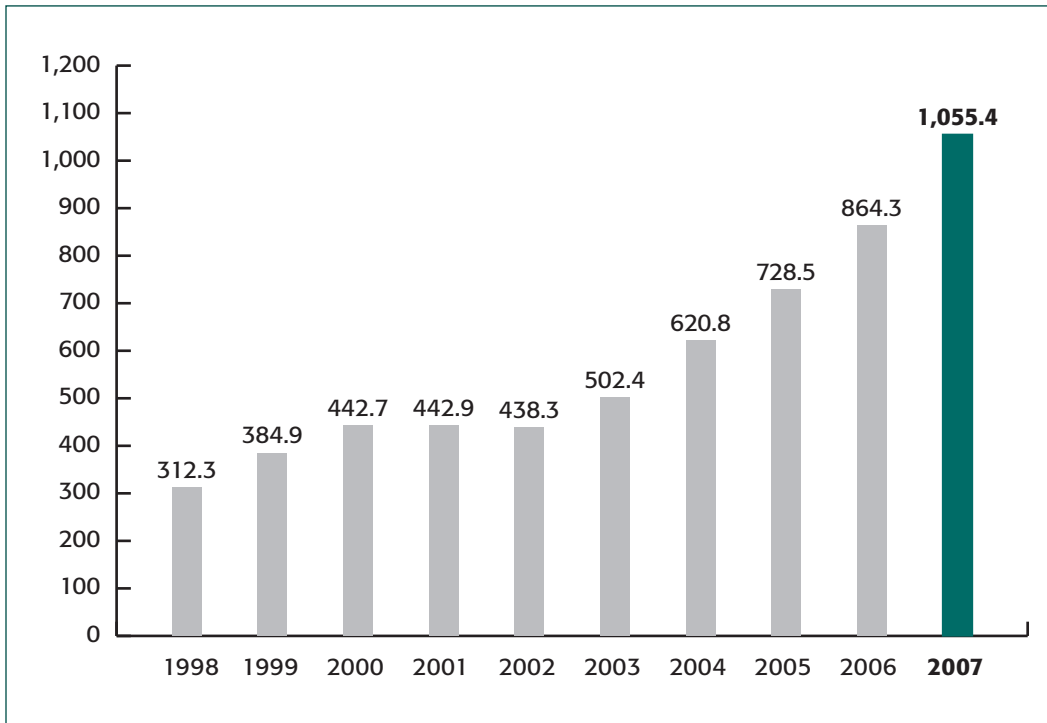
A total of 4,905 employees enrolled in the Commonwealth's 457 Deferred Compensation Plan during the 2006-2007 fiscal year. The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) became effective January 1, 2002, allowing increased tax-deferred savings and to have increased portability of benefits. Contributions to the plan during FY 2007 increased to \$109,320,357 from \$107,199,887 in FY 2006.

EGTRRA also made the 457 Plan attractive for employees of colleges and universities by removing the coordination between 457 Plans and 403(b) tax-deferred accounts. From the effective date of EGTRRA to June 30, 2007, the number of college and university employee plan accounts increased from 287 in FY 2001 (the baseline year) to 2,766 in FY 2007.

The 2001 legislation also allowed 457 Plan participants to use monies in their accounts to purchase eligible service in their defined benefit plan. During the fiscal year ended June 30, 2007, 102 plan participants used the trustee-to-trustee transfer provision to buy VRS service credit with \$630,204 transferring from the 457 Plan to the defined benefit plan.

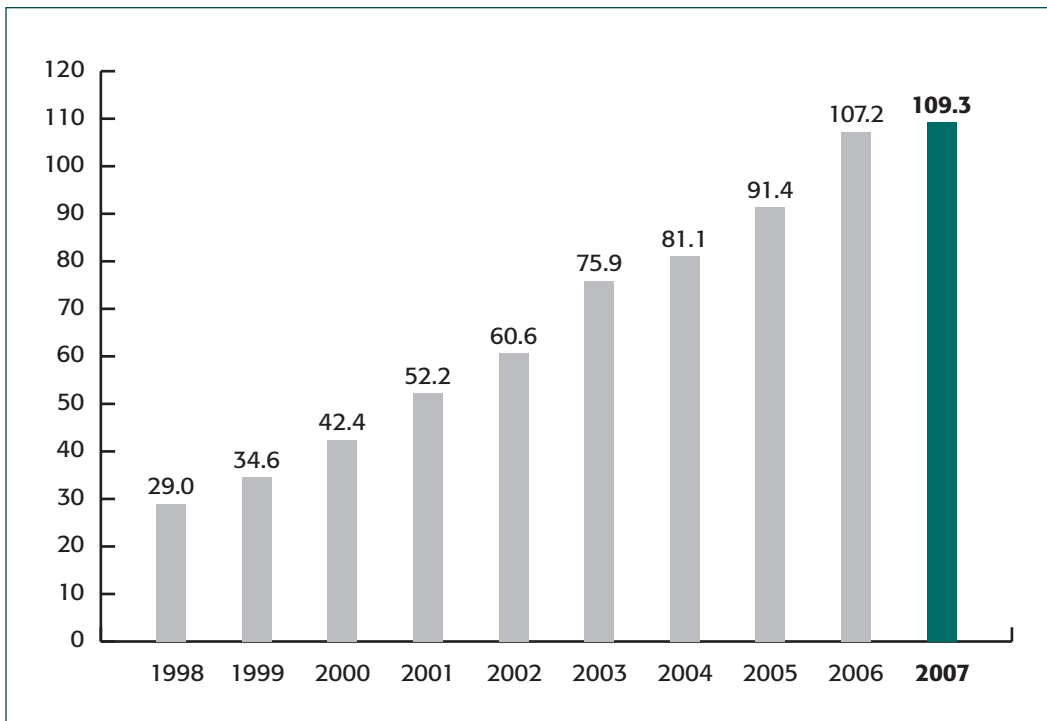
Deferred Compensation Plan Assets

(MILLIONS OF DOLLARS)



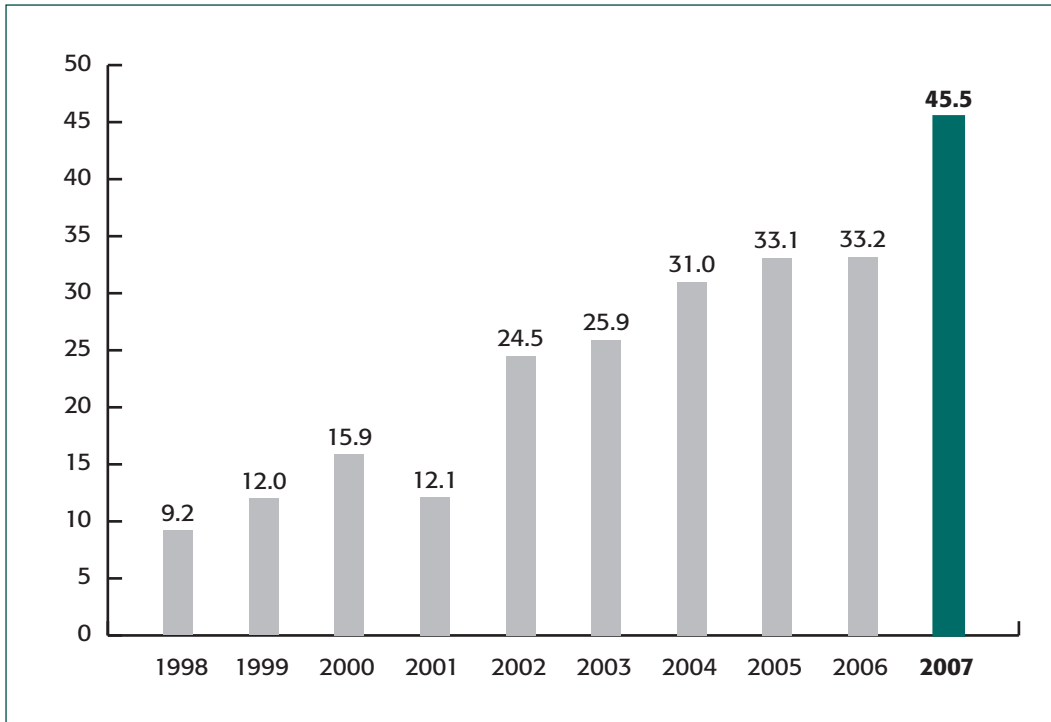
Contributions to the Deferred Compensation Plan

(MILLIONS OF DOLLARS)

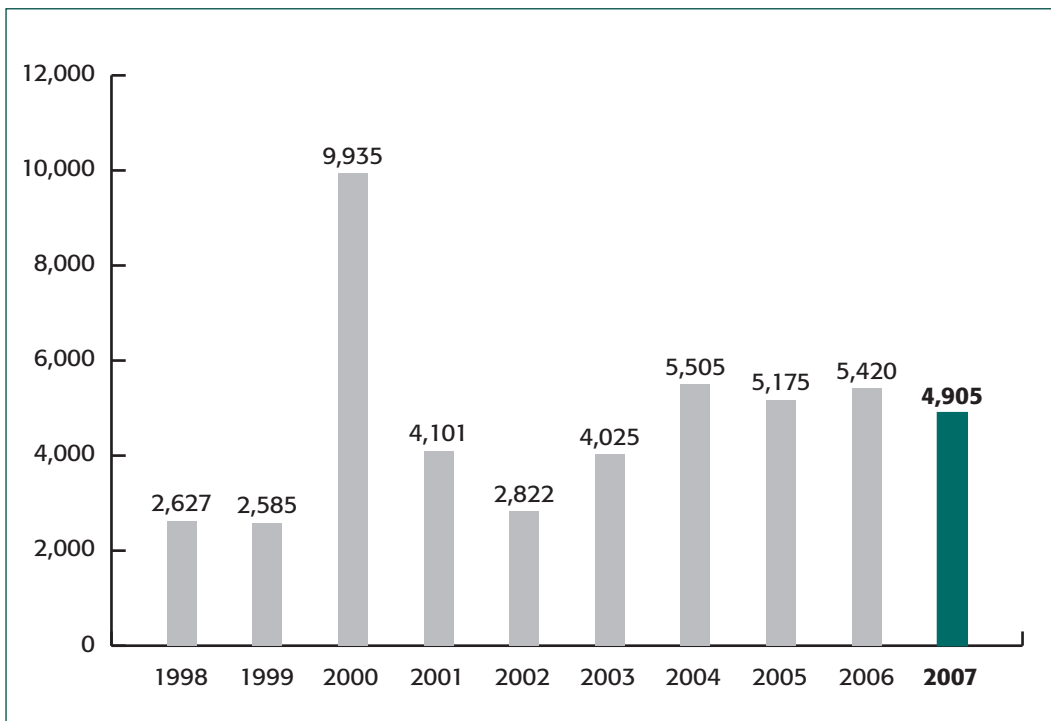


Distributions from the Deferred Compensation Plan

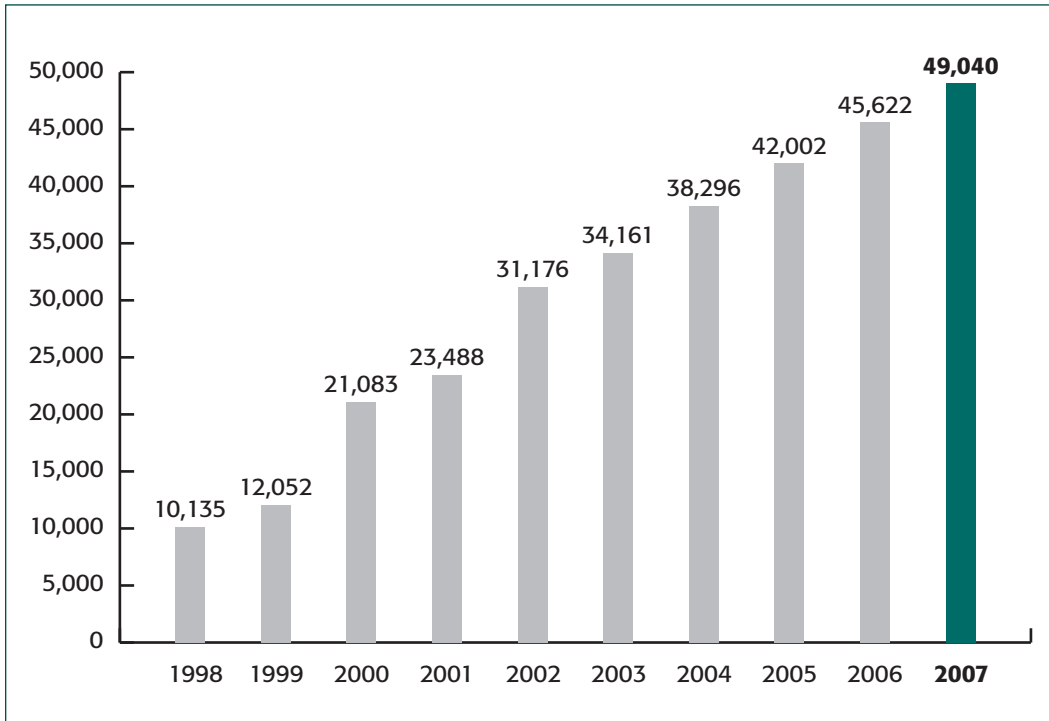
(MILLIONS OF DOLLARS)



New Enrollments in the Deferred Compensation Plan



Active and Inactive Deferred Compensation Plan Participants



Total Participant Accounts in Each Fund Option

Fund Name	Total Participant Accounts*	Fund Name	Total Participant Accounts*
Income & Growth Fund	5,618	Real Estate Investment Trust Index Fund	8,100
Balanced Growth Fund	10,651	Money Market Fund	3,331
Long-Term Growth Fund	8,115	Active Inflation-Protected Bond Fund	2,102
Bond Index Fund	5,548	Active Bond Fund	4,428
S&P 500 Index Fund	23,683	Active High-Yield Bond Fund	1,757
Russell 1000 Value Index Fund	7,650	Active Small/Mid Cap Equity Fund	6,465
Russell 1000 Growth Index Fund	3,740	Active Global Equity Fund	3,563
Russell 3000 Index Fund	1,518	Stable Value Fund	19,158
Small/Mid Cap Equity Index Fund	8,228	Self-Directed Brokerage	91
International Equity Index Fund	9,116		

* The number of participant accounts will exceed the number of participants since a participant may invest in more than one fund.

Plan Assets

Accumulation Plan Assets represent funds invested among the 18 core investment options and self-directed brokerage option. The following schedule shows how these investments are distributed among the available options:

Deferred Compensation Accumulation Plan Assets

	FY 2007	FY 2006
Allocation by Fund Manager:		
Income & Growth Fund	\$ 17,254,740	\$ 13,472,331
Balanced Growth Fund	111,804,977	99,966,407
Long-Term Growth Fund	34,976,826	25,656,207
Bond Index Fund	33,381,479	29,615,901
S&P 500 Index Fund	281,670,190	233,056,607
Russell 1000 Value Index Fund	56,082,530	36,455,838
Russell 1000 Growth Index Fund	15,975,159	11,102,812
Russell 3000 Index Fund	5,988,328	3,190,547
Small/Mid Cap Equity Index Fund	54,266,743	44,322,834
International Equity Index Fund	63,863,761	40,728,065
Real Estate Investment Trust Index Fund	39,766,497	34,282,602
Money Market Fund	14,863,639	11,075,499
Active Inflation-Protected Bond Fund	8,026,222	6,776,266
Active Bond Fund	16,269,839	14,350,084
Active High-Yield Bond Fund	3,992,471	2,887,450
Active Small/Mid Cap Equity Fund	48,957,934	44,109,083
Active Global Equity Fund	19,194,218	10,221,140
Stable Value Fund (Galliard)	222,585,805	198,414,360
Self-Directed Brokerage	6,503,579	4,588,478
Total Accumulation Plan Assets:	<u>\$ 1,055,424,937</u>	<u>\$ 864,272,511</u>

Description of Funds

Tier I: Passively Managed Asset Allocation Funds

Income & Growth Fund: Seeks to provide income and a modest level of capital growth by investing in a combination of bonds and stocks that is anticipated to provide long-term total returns that are slightly higher than inflation with the possibility of occasional short-term losses.

U.S. Bonds - 75.0%
 U.S. Stocks - 22.0%
 Foreign Stocks - 3.0%

Balanced Growth Fund: Seeks to provide income and a modest level of capital growth by investing in a combination of bonds and stocks that is anticipated to provide long-term total returns that are higher than inflation with the possibility of short-term losses.

U.S. Bonds - 50.0%
 U.S. Stocks - 43.0%
 Foreign Stocks - 7.0%

Long-Term Growth Fund: Seeks to provide capital growth by investing in a combination of bonds and stocks that is anticipated to provide long-term total returns that are higher than inflation with the possibility of significant short-term losses.

U.S. Stocks - 64.0%
 U.S. Bonds - 25.0%
 Foreign Stocks - 11.0%

Tier II: Passively Managed Funds

Bond Index Fund: Seeks to track the total return performance of the Lehman Brothers Aggregate Bond Index. This index is comprised of government, corporate, mortgage-backed and asset-backed securities.

Mortgage-Backed Securities - 37.7% CMBS - 5.0%
 Treasury - 24.2% Non-US Credit (Yankee) - 3.3%
 Agency - 10.7% Utility - 1.8%
 Industrial - 8.7% Asset-Backed Securities - 0.9%
 Finance - 7.7%

S&P 500 Index Fund: Seeks to track the performance of the Standard & Poor's 500 Index. This index is comprised of 500 widely held U.S. stocks chosen by Standard & Poor's.

Financials - 21.0% Consumer Discretionary - 10.1%
 Information Technology - 15.6% Consumer Staples - 9.4%
 Health Care - 11.8% Telecommunications Services - 3.7%
 Industrials - 11.0% Utilities - 3.5%
 Energy - 10.8% Materials - 3.1%

Russell 1000 Value Index Fund: Seeks to track the performance of the Russell 1000 Value Index. This index is comprised of stocks in the Russell 1000 that have lower price-to-book ratios and lower forecasted growth values.

Financials - 33.8% Health Care - 6.8%
 Energy - 13.2% Telecommunications Services - 6.5%
 Industrials - 10.4% Utilities - 6.0%
 Consumer Discretionary - 8.2% Materials - 4.0%
 Consumer Staples - 7.5% Information Technology - 3.6%

Russell 1000 Growth Index Fund: Seeks to track the performance of the Russell 1000 Growth Index. This index is comprised of stocks in the Russell 1000 that have higher price-to-book ratios and higher forecasted growth values.

Information Technology - 27.0% Energy - 7.9%
 Health Care - 16.0% Financials - 7.4%
 Consumer Discretionary - 13.7% Materials - 3.0%
 Industrials - 12.9% Utilities - 1.6%
 Consumer Staples - 9.6% Telecommunications Services - 0.9%

Russell 3000 Index Fund: Seeks to track the performance of the Russell 3000 Index. This index is comprised of the 3,000 largest stocks in the U.S. Market.

Financials - 20.7% Energy - 10.1%
 Information Technology - 15.5% Consumer Staples - 8.1%
 Industrials - 11.9% Utilities - 3.7%
 Health Care - 11.5% Materials - 3.6%
 Consumer Discretionary - 11.4% Telecommunications Services - 3.5%

Small/Mid Capitalization Equity Index Fund: Seeks to track the performance of the Russell Small Capitalization Completeness Index. This index is a measure of the small to mid-capitalization sector of the U.S. Stock Market.

Financials - 21.3% Energy - 7.5%
 Consumer Discretionary - 15.9% Materials - 5.5%
 Information Technology - 15.1% Utilities - 4.4%
 Industrials - 14.3% Consumer Staples - 2.9%
 Health Care - 10.5% Telecommunications Services - 2.6%

International Equity Index Fund: Seeks to track the performance of the Morgan Stanley Capital International Europe, Australasia, Far East Index (MSCI EAFE). This index is comprised of approximately 1,000 stocks in 21 countries in Europe and the Pacific Basin.

Financials - 28.7% Health Care - 6.4%
 Industrials - 12.0% Information Technology - 5.6%
 Consumer Discretionary - 11.7% Telecommunications Services - 5.4%
 Materials - 9.4% Utilities - 5.2%
 Consumer Staples - 7.8% Other - 0.3%
 Energy - 7.5%

Description of Funds, continued

Real Estate Investment Trust Index Fund: Seeks to track the performance of the Dow Jones Wilshire REIT Index. This index is a market capitalization weighted index of publicly traded REITs whose charter is the equity ownership and operation of commercial real estate.

Apartments - 21.1%	Diversified - 7.7%
Retail Malls - 16.3%	Industrial Mixed - 6.0%
Office - 13.5%	Self Storage - 4.4%
Retail Strip Centers - 11.2%	Manufactured Homes - 0.6%
Hotels - 10.4%	Factory Outlets - 0.4%
Industrial - 8.4%	

Tier III: Actively Managed Funds

Money Market Fund: Seeks to provide short, medium and long-term returns that provide for a high level of current income while preserving capital.

CDs, ECDs, TDs, BAs - 30.3%	Commercial Paper - 15.1%
Repurchase Agreements - 24.9%	Adjustable Rate ABS - 7.4%
Floating Rate Corporate Notes - 21.1%	Other Short-Term Instruments - 1.2%

Active Inflation-Protected Bond Fund: Seeks to provide inflation protection and income consistent with investment in inflation-indexed securities and seeks to provide long-term returns that exceed the performance of the Lehman Brothers U.S. Treasury Inflation Notes Index. This index is a measure of the inflation-indexed sector of the U.S. Bond Market.

U.S. Treasury/Agency - 99.9%
Other - 0.1%

Active Bond Fund: Seeks to provide long-term returns that exceed the performance of the Lehman Brothers Aggregate Bond Index. This index is comprised of government, corporate, mortgage-backed and asset-backed securities.

Mortgage-Backed Securities - 53.0%	Emerging Markets (\$US) - 5.0%
U.S. Government/Agency - 23.0%	Non-U.S. Developed - 1.0%
Net Cash & Equivalents - 12.0%	Other - 1.0%
Credit - 5.0%	

Active High Yield Bond Fund: Seeks to provide a high level of current income and provide long-term returns that exceed the performance of a custom benchmark consisting of 95% Lehman Brothers High-Yield ex-CCC Index and 5% Lehman Brothers 1-3 Year Treasury Index.

Communication - 19.7%	Capital Goods - 6.6%
Consumer, Cyclical - 18.6%	Finance - 4.4%
Consumer, Non-Cyclical - 11.2%	U.S. Treasury/Agency - 4.1%
Utilities - 11.0%	Technology - 4.0%
Basic Industry - 9.1%	Other - 3.2%
Energy - 8.1%	

Active Small/Mid Capitalization Equity Fund: Seeks to provide long-term returns that exceed the performance of the Russell Small Capitalization Completeness Index. This index is a measure of the small to mid-capitalization sector of the U.S. Stock Market.

Financials - 20.0%	Energy - 7.5%
Consumer Discretionary - 15.9%	Materials - 6.5%
Information Technology - 15.8%	Consumer Staples - 3.7%
Industrials - 13.3%	Utilities - 3.6%
Health Care - 10.8%	Telecommunications Services - 2.9%

Active Global Equity Fund: Seeks to provide long-term growth of capital with current income and long-term returns that exceed the performance of the MSCI World Index. This index is a measure of the global developed market.

Europe - 46.7%	Cash & Equivalents - 5.4%
United States - 22.0%	Non-U.S. Americas - 5.1%
Asia/Pacific Basin - 19.6%	Other - 1.2%

Stable Value Fund: Seeks to provide a safety of principal and a stable credited rate of interest while generating competitive returns over time compared to other conservative investments, such as money market funds or short-term yields available in the fixed-income (bond) market.

JP Morgan Chase Bank Security Backed Contract - 22.5%
Union Bank of Switzerland AG Security Backed Contract - 22.2%
Royal Bank of Canada Security Backed Contract - 22.2%
AIG Financial Products Security Backed Contract - 22.2%
Wells Fargo Stable Return Fund - 10.9%

Tier IV: Self-Directed Brokerage Option

The Self-Directed Brokerage Account (SDBA) option offered through Ameritrade Corporate Services, a division of Ameritrade, Inc., allows investors to elect from thousands of mutual funds in addition to the core investment options in Tier I, Tier II and Tier III. The SDBA option is for knowledgeable investors who acknowledge and understand the risks associated with the mutual fund investments contained within this option. (Participants cannot invest in individual securities such as stocks, bonds or options.) In addition to the annual recordkeeping and communication services fee, there is a plan fee of \$15 per quarter, as well as transaction fees charged by Ameritrade and investment management fees charged by the investment managers.

Investment Option Performance Summary

Below are totals for the period ending June 30, 2007

(RETURNS GREATER THAN ONE YEAR ARE ANNUALIZED)

Investment Options	1 Year	3 Years	5 Years	Expense Ratio
Tier I: Passively Managed Asset Allocation Funds ¹				
Income & Growth Fund	9.69%	6.38%	6.51%	0.08%
Benchmark (75% Lehman Bros. Aggregate Bond Index, 22% Russell 3000, 3% MSCI EAFE)	9.69%	6.39%	6.55%	
Balanced Growth Fund	13.42%	8.88%	8.52%	0.08%
Benchmark (50% Lehman Bros. Aggregate Bond Index, 43% Russell 3000, 7% MSCI EAFE)	13.42%	8.89%	8.60%	
Long-Term Growth Fund	17.25%	11.40%	10.45%	0.08%
Benchmark (25% Lehman Bros. Aggregate Bond Index, 64% Russell 3000, 11% MSCI EAFE)	17.22%	11.39%	10.58%	
Tier II: Passively Managed Funds ^{1,2}				
Bond Index Fund	6.11%	3.97%	4.50%	0.06%
Lehman Bros. Aggregate Bond Index	6.12%	3.98%	4.48%	
S&P 500 Index Fund	20.58%	11.69%	10.72%	0.02%
S&P 500 Index	20.59%	11.68%	10.71%	
Russell 1000 Value Index Fund	21.86%	15.90%	13.29%	0.09%
Russell 1000 Value Index	21.87%	15.93%	13.31%	
Russell 1000 Growth Index Fund	18.93%	8.63%	9.17%	0.09%
Russell 1000 Growth Index	19.04%	8.70%	9.28%	
Russell 3000 Index Fund	20.08%	12.44%	11.44%	0.08%
Russell 3000 Index	20.07%	12.44%	11.53%	
Small/Mid Cap Equity Index Fund ³	18.96%	15.51%	15.28%	0.11%
Russell Small Cap Completeness Index	18.88%	15.46%	15.35%	
International Equity Index Fund ^{4,5}	27.06%	22.26%	16.96%	0.14%
MSCI EAFE Index	27.00%	22.24%	17.73%	
Real Estate Investment Trust Index Fund	11.41%	21.87%	18.75%	0.20%
Dow Jones Wilshire REIT Index	11.68%	22.26%	19.25%	

Investment Option Performance Summary, continued

Investment Options	1 Year	3 Years	5 Years	Expense Ratio
Tier III: Actively Managed Funds				
Money Market Fund	5.37%	3.90%	2.83%	0.12%
91-Day Treasury Bill Average	5.26%	3.98%	2.85%	
Active Inflation-Protected Bond Fund	3.94%	3.75%	5.88%	0.08%
Lehman Bros. US Treas. Inflation Notes Index	3.99%	3.80%	6.03%	
Active Bond Fund	5.21%	3.97%	4.78%	0.43%
Lehman Bros. Aggregate Bond Index	6.12%	3.98%	4.48%	
Active High-Yield Bond Fund ⁷	9.15%	6.90%	8.17%	0.13%
Benchmark (95% Lehman Bros. High Yield ex-CCC, 5% Leman Bros. 1-3 Year Treasury Index)	10.28%	8.13%	10.23%	
Active Small/Mid Cap Equity Fund ^{1, 3}	15.42%	12.76%	14.16%	0.57%
Russell Small Cap Completeness Index	18.88%	15.46%	15.35%	
Active Global Equity Fund ⁴	28.30%	22.11%	19.71%	0.48%
MSCI World Index	23.59%	16.73%	14.00%	
Stable Value Fund ⁶	5.46%	5.39%	5.28%	0.18%
The Stable Value Fund current yield as of June 30, 2007 was 5.40% ⁷				

¹ The VRS Defined Contribution Plans purchase units in various State Street Global Advisors (SSgA) Series A or Series T collective trust funds in order to provide plan participants with the ability to purchase and redeem units on a daily basis. SSgA Series A or Series T Funds invest in other SSgA collective trust funds referred to as Base Funds.

² Inception dates shown reflect the inception dates of the Base Funds. Performance returns for the Series A Funds have been linked to those Base Funds' returns. The actual performance for the Base Funds has been restated to reflect the Plans' investment management fees. Inception dates for the Series A Funds commenced as follows:

SSgA Bond Index Series Class A	10/97	SSgA REIT Index Series Class A	5/01
SSgA S&P 500 Index Series Class A	3/96	SSgA Russell Small Cap Completeness Index Series Class A	9/97
SSgA Russell 1000 Value Index Series Class A	3/99	SSgA EAFE Index Series Class A	1/97
SSgA Russell 1000 Growth Index Series Class A	8/99	SSgA Russell 3000 Index Series Class A	6/97

³ Equity securities of companies with relatively small market capitalization may be more volatile than securities of larger, more established companies.

⁴ Foreign investments involve special risks, including currency fluctuations and political developments.

⁵ Inception dates shown reflect the inception dates of the Base Fund. Performance returns for the Series Class T Fund have been linked to the returns of the Series Class A and Base Funds. The actual performance for the Base Fund has been restated to reflect the Plans' investment management fees. The inception date of VRS' participation in the Series Class T Fund was April 21, 2003.

⁶ Performance returns have been linked to the previous investment manager. Returns prior to May 5, 2003 represent performance by MetLife.

⁷ The estimated yield range is provided to help participants make choices concerning their investment options. **There is no guarantee that the Fund will earn the projected estimated yield.**



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