2009 Annual Report

Office of the State Treasurer

State of Vermont

Issued January 2010

Jeb Spaulding
State Treasurer

The Vermont State Treasurer's Office Strives to:

- Give Vermont taxpayers an excellent value.
- Offer the best customer service possible.
- Deliver the highest quality operational services.
- Create a productive employee work environment.

Office of the State Treasurer
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Montpelier, Vermont 05609
www.VermontTreasurer.gov

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Our Commitment to Vermonters

The State Treasurer's Office manages money that belongs to all citizens of Vermont. The Treasurer and staff are committed to doing this honestly, efficiently, responsibly, and professionally. The Treasurer's office operates as a business, serving the needs of Vermonters while working to save the taxpayers money and earn the highest possible investment returns in its funds within acceptable risk parameters.

Office of the State Treasurer
Mission Statement

To manage the financial resources within our purview effectively and efficiently and to promote prudent financial practices in the State of Vermont.

Vision Statement

The overall vision of the State Treasurer's Office is to be the best office of the treasury in the U.S.A. This vision is further defined to state that the Treasurer's Office staff will:

- **Give Vermont taxpayers an excellent value.**

  Excellent value to Vermont taxpayers implies highly competent investment and funds management; and initiative and creativity to "leave no stone unturned" with regard to either maximizing returns on investments or achieving maximum savings without compromising other office objectives.

- **Offer the best customer service possible.**

  Excellent customer service implies an effort to understand customer needs, a timely and appropriate response, and a proactive approach to solving problems.

- **Deliver the highest quality operational services.**

  Providing high-quality services requires the pursuit of operating practices within the office that utilize valuable resources efficiently.

- **Create a productive employee work environment.**

  A productive employee work environment implies teamwork, satisfied and motivated staff, and an appropriate set of core objectives and values.

CORE VALUES & SUPPORTIVE BEHAVIORS

Integrity above all
Supported by honesty, fairness, trust, and self-reflection.

A strong team spirit
Supported by open communication, mutual respect and support, and consistent treatment of all.

Desire for excellence
Supported by professionalism, accountability, and pride in work.

Letter of Transmittal

TO: Members of the General Assembly
Honorable James H. Douglas, Governor
Citizens of Vermont

I respectfully submit the 2009 Annual Report for the Office of the Vermont State Treasurer. This document serves to fulfill statutory responsibilities, provide useful information on treasury-related activities, and highlight the achievements of this office. Despite the tremendous financial challenges of this past year, we have accomplished a great deal. That is a real testament to the hardworking and professional staff in this office.

The economic recession and credit crisis has impacted the entire spectrum of Vermont life—affecting taxpayers, the public and private sector workforce, and all aspects of government services and operations. Protecting this state's assets during these difficult times has been my highest priority. The Office of the State Treasurer has exercised prudence, building on years of sound financial practices while implementing carefully considered risk management strategies. As you will see in this report, Vermont's conservative debt management practices and hard-earned high credit rating paid off in these tough economic times. While many states and local governments were not able to obtain credit, Vermont was able to issue bonds for needed capital projects at favorable rates. While the pension funds suffered losses consistent with the massive market meltdown, we remained disciplined investors and have been able to benefit from the current upturn in the markets. Even as Vermont was able to avoid some of the investment losses in operating funds experienced in other states, we made a concerted effort to revamp our portfolio, increasing the collateralization of deposits as appropriate while investing in more conservative financial instruments. We continue to retool our cash management projection techniques so that we can optimize our banking relationships and make the most of scarce resources. As the State has taken action to meet these challenges, the Treasurer's Office has played an integral role. A number of significant accomplishments were made while wrestling with the larger economic issues.

Vermont's conservative debt management practices and hard-earned high credit rating paid off in these tough economic times.

Key Accomplishments

- The Treasurer's Office worked with the Administration, the State Legislature and the Vermont State Employees' Association to implement a retirement incentive program. The Retirement Division of the State Treasurer's Office mailed letters to approximately a thousand eligible employees and geared up for the surge in retirements, offering informational workshops and individual counseling sessions to interested employees. In all, 243 employees took advantage of the incentive program. This initiative allowed the State to decrease the size of its workforce, but in a way that lessened the economic hardship on employees caused by layoffs, while achieving needed budgetary savings.

This initiative allowed the State to decrease the size of its workforce, but in a way that lessened the economic hardship on employees caused by layoffs, while achieving needed budgetary savings.

- Following completion of a transportation study by my office on funding options for Vermont's bridges and culverts, the legislature created a motor fuel transportation infrastructure assessment. The added revenue takes some financial pressure off of the State for funding a backlog of badly needed projects by providing support for bonding or pay-as-you-go funding.

The recent market upturn notwithstanding, there is a new reality and a new set of challenges. Financial commitments for governmental programs are growing much faster than the rate of revenue growth and budgets will be squeezed.

Vermonters responded vigorously in 2009 to the opportunity to invest in the State. A March sale by my office of approximately $50 million in General Obligation bonds was offered first to Vermont residents and businesses in increments as low as $1,000. The offering sold out in less than three hours.

A new Vermont Manager Program was initiated in 2009 by the Vermont Pension Investment Committee. The program aims to utilize locally provided investment management services in a "buy local" approach to bolstering Vermont firms. Following a competitive process, two Vermont firms were selected to manage approximately $42 million in assets of the roughly $2.9 billion in assets for the State pension systems. Both the selected companies foresee positive growth in their staffing base as a result of securing these contracts.

The search for owners of unclaimed property continued in 2009. There were 8,798 claims paid for more than $5.6 million—an increase of $1.2 million over the previous year. We also continued gains in the addition of new holders of unclaimed property to our systems. Holders reported $8.4 million worth of unclaimed funds to the State in fiscal year 2009.

On the financial literacy front, a MoneyEd initiative implemented in spring 2009 resulted in the production and distribution of a 30-minute personal finance program that was aired on 23 Vermont public access stations. This work was used to develop a financial readiness workshop for deploying Vermont National Guard troops. My office conducted this workshop at all Yellow Ribbon briefing events, reaching more than 400 soldiers and their family members. We also introduced the first-ever Vermont Championship Reserve Cup Challenge for high school students. The competition promotes student interest in and knowledge of personal finance, economics, and consumer affairs.

Failure to address the issue of the sustainability of our public retirement plans now will surely lead to larger problems later and the need for more draconian steps that fail both the employees and the taxpayers.

As we move forward, we need to recognize that all governments, including Vermont, will be facing tough times for years to come. The recent market upturn notwithstanding, there is a new reality and a new set of challenges. Financial commitments for governmental programs are growing much faster than the rate of revenue growth and budgets will be squeezed. In fact, as I write this report, Vermont is facing an estimated $150 million General Fund budgetary deficit in fiscal year 2011, which will grow significantly in years to come if changes are not made. While the economic crisis requires short-term remedial steps, the sustainability of essential services at a price that taxpayers can afford will also require new and innovative long-term solutions.

Financial commitments for pensions and the funding of health care for future retirees will continue to grow. I will continue to advocate for the full funding of the actuarially recommended contributions even as budget constraints create pressures to reduce or limit full funding. However, as a fiduciary and an advocate for providing a solid foundation for retirement security, I also recognize the need to provide a sustainable plan that is fair to workers and other taxpayers. Consider these sobering statistics:

- In fiscal year 2008, the State's combined actuarial pension contribution of $66.3 million represented 5 percent of General Fund revenues. The State's projected actuarial contribution for fiscal year 2011, assuming no changes, represents about 9.5 percent of the expected General Fund revenues.

- An investment upturn will not get the State out of this fiscal problem. Our actuaries estimate it will take more than 20 years at our current actuarial investment rate of return of 8.25 percent to get back to the fiscal year 2008 funding level.

- The rate of growth in retirees in the State employees' and teachers' systems is outpacing the rate of growth in active members. Pension benefit payouts for these groups have increased by roughly $10-11 million each year in recent years and is now increasing by $15-16 million.
- The State's combined actuarially required contribution for both the State employees' and teachers' systems for fiscal year 2010 is $73.5 million. Absent any changes being implemented, the required contribution will grow to $105.1 million in 2011, almost a $32 million increase in one year increase. For the State employees' system, the fiscal year 2011 recommendation alone represents a 328 percent increase compared to fiscal year 2003.
- Currently, the State does not prefund its post-employment benefits, notably medical. By 2020 the actuary estimates health care pay-as-you-go payments for teachers will double to $38.3 million and double again to $77.4 million by 2040. For the State system, the pay-as-you-go payments will reach $46.5 million in 2020 and $73.8 million by 2040.

As Vermont takes more steps to come to terms with economic and budgetary stresses, the Treasurer's Office remains committed to working with its partners to achieve long-term solutions.

The 2009 General Assembly created the Commission on the Design and Funding of Retirement and Retiree Health Benefits Plans for State Employees and Teachers. I was appointed chair of the commission by the legislature. Following a six-month concerted process of fact-finding and exploration, the commission completed its report and issued its recommendations (the executive summary is included in the appendices of this report). The recommendations attempt to strike a balance between public policy and the economic context in which the current benefit structure operates. Failure to address the issue of the sustainability of our public retirement plans now will surely lead to larger problems later and the need for more draconian steps that fail both the employees and the taxpayers. Change will occur, either by careful long-term planning, by default, or in crisis. Clearly, there are no easy solutions, but there are fiscally and socially responsible steps we can take. While the commission believes that these recommendations provide a solid course of action, we also recognize that there is a range of options inherent in each, with varying impacts on the overall cost of benefits. We are hopeful the commission report will provide a foundation for meaningful dialogue within which varying proposals can be reviewed.

As Vermont takes more steps to come to terms with economic and budgetary stresses, the Treasurer's Office remains committed to working with its partners to achieve long-term solutions. My staff and I are available to discuss the information in this report and welcome your inquiries and comments. You will find a great deal of additional information by visiting our web site at www.VermontTreasurer.gov. I look forward to working with all of you in the upcoming 2010 legislative session.

Sincerely,

Jeb

Jeb Spaulding
State Treasurer

About the Treasurer's Office

Administrative & Service Duties

The State Treasurer's Office serves as the State's banker and chief investment officer. We handle money that belongs to all of the citizens of Vermont. We are committed to managing these funds honestly, efficiently, and responsibly, and to maintaining Vermont's hard-earned reputation as a fiscally sound and disciplined state. Specific administrative and service duties as prescribed by State statutes include:

- **Investment of State funds.**
- **Issuing all State bonds authorized by the General Assembly.**
- **Serving as the central bank for State agencies.**
- **Management of the State's cash balances, processing of checks, and the reconciliation of payroll and vendor checks.**

- **Safeguarding and return of unclaimed or abandoned financial property, which is held in trust by the State until the rightful owner can be located.**
- **Administration of three major pension plans, the deferred compensation plan, and the defined contribution plan for State employees, teachers, and participating municipalities.**

Executive Office
(802) 828-1452

Jeb Spaulding
State Treasurer

Beth Pearce
Deputy Treasurer

Barbara Agnew
Executive Staff Assistant

Office Organization

The State Treasurer's Office is organized into an executive office and five divisions. The executive office is responsible for overall strategic planning, legislative initiatives, constituent relations, debt management, financial literacy, and supervision of the divisions.

The Treasury Operations Division is responsible for the State's banking, cash management, and financial transaction services. The Retirement Division administers three public retirement systems authorized by the legislature (see report section on Vermont Retirement Systems). Debt Management and Investment Services provides cash, investment, and debt management for the State of Vermont and the three pension systems administered by the office. The Unclaimed Property Division serves as the caretaker of abandoned or unclaimed financial property, while seeking to return it to its proper owner. Technology Services is responsible for developing and maintaining automated systems, providing appropriate access to information, maintaining the office web site, and maintaining the overall security of the office network and automated interactions with other State department and entities outside of State government.

Employee of the Year

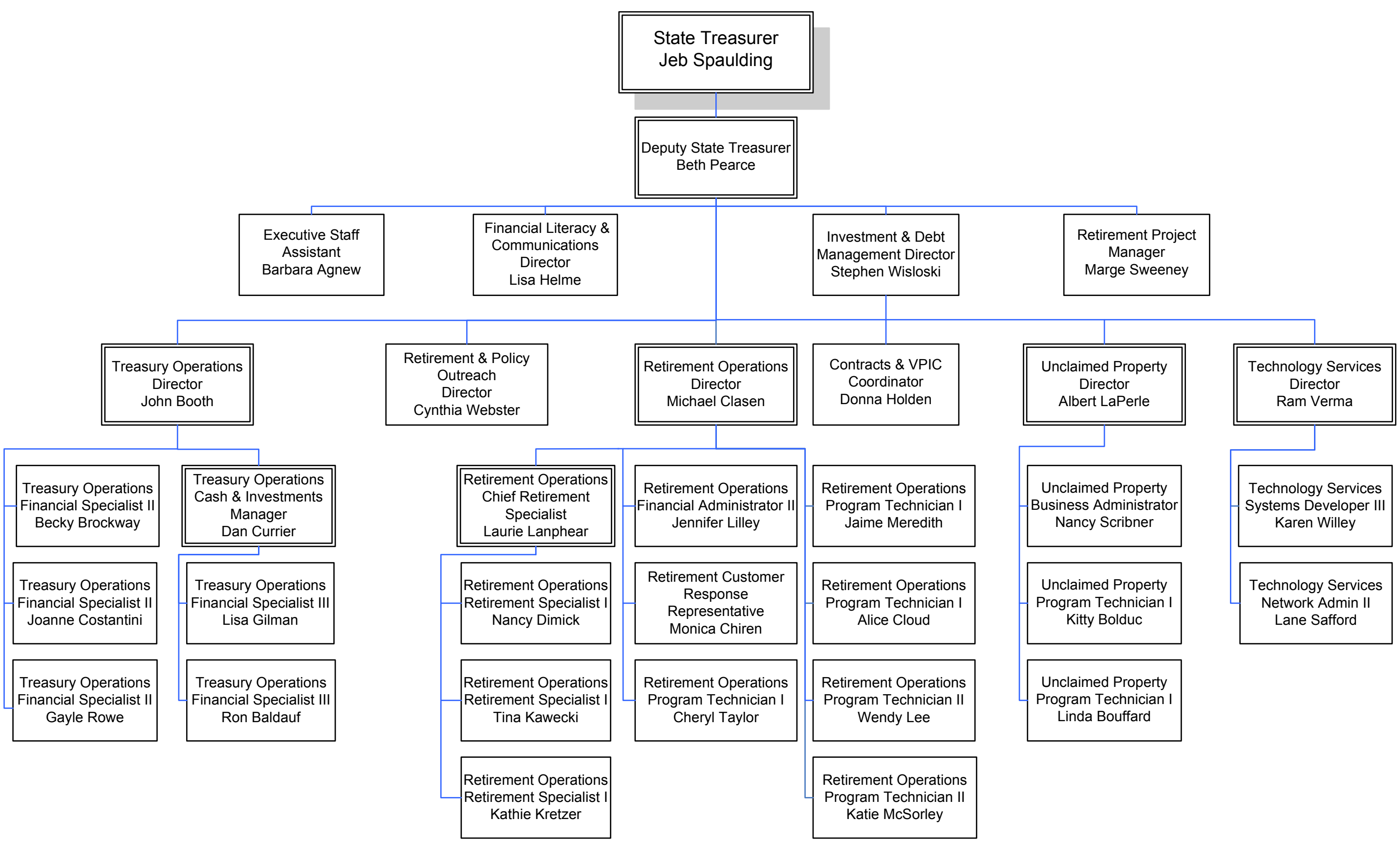
The State Treasurer's Office "Employee of the Year" selection is Dan Currier, the Treasury Operations Cash Investment Manager. At the May 6 public service recognition week luncheon, Dan was praised for his hard work and creative approaches to his job. "These unprecedented economic times have placed new demands on public finance and treasury staff. Dan is proactive in meeting these challenges, while managing the State's $180 million of operating cash. With an eye toward safeguarding taxpayer's funds, he designed new cash management forecasting tools and updated collateralization practices to anticipate problems and reduce risk while maximizing returns. He volunteered to assist with the compilation of pension fund financial statements, and credit card security compliance. He worked diligently with his supervisor, John Booth, and other business partners to ensure we maintain a prudent and disciplined approach in these volatile times."

Treasury Operations Cash Investment Manager Dan Currier has worked more than 11 years for the State. He was named the 2009 Treasurer's Office Employee of the Year.

Organizational Chart

There are 34 staff members working within the State Treasurer's Office. Below is the office organizational chart. The organizational chart and staff listings in this report are effective as of January 1, 2010.

Vermont State Treasurer's Office



Vermont Retirement Systems

Retirement plans administered by the State Treasurer's Office serve approximately 45,000 active and retired members. These plans serve members of the Vermont State Employees' Retirement System (VSERS), Vermont State Teachers' Retirement System (VSTRS), and the Vermont Municipal Employees' Retirement System (VMERS). Each system is statutorily overseen by a board of trustees.

Boards' Accomplishments & Updates

The boards have a great responsibility that entails balancing the needs of their members with the escalating cost of addressing those needs, while providing secure and adequate benefits after retirement. With more than 12,245 retirees currently receiving pensions totaling over $174.7 million annually, the task is challenging. In addition to the existing retirees, the demographics of the three systems reflect that another 8,830 members will be eligible to retire within the next five years.

Boards Administration
(802) 828-2302

Cynthia Webster
Executive Secretary of the Boards and Director of Retirement Policy & Outreach

Monica Chiren
Assistant to the Boards

ACCOMPLISHMENTS IN 2009

- The teachers' board successfully designed and implemented a new 403(b) Investment Program for school employees across the State. The initial enrollment endeavor resulted in 25 supervisory unions adopting the TRS 403(b) program. During the first quarter of activity, 884 participants elected to participate, and plan assets totaled $1.69 million by the end of March, 2009. By the end of September, 2009, the participant count had grown to 1,139 and the assets had grown to $6.54 million.

- The teachers' board successfully advocated for full actuarial funding of the retirement system for the fourth year in a row.

- With the assistance of the Vermont Education Health Initiative, through which the teachers' board obtains the medical insurance that is offered to retired teachers, premiums for the medical plans available to Medicare-eligible and non-Medicare eligible retirees have remained at the same level for two years in a row.

- The State board expanded the options available to participants in the State of Vermont Deferred Compensation (457) Plan by offering Reality Investment. Reality Investment allows a participant to enjoy three levels of investment advice. The first is free, and simply provides generic information about diversification; the second level charges a flat fee to have access to a sample portfolio based on risk and reward tolerance; and the third level is full investment advice and assistance for a fee that is based on a percentage of assets. Participation at all levels is voluntary.

- The State board successfully advocated for enabling legislation to allow the unfunded liability of the retirement system to be re-amortized over a 30-year period. Re-amortization of a system's unfunded liability in the final years of the amortization period is a common practice for public retirement systems across the country and typically results in a reduction in the amount of the State's actuarially required contribution in the future.

- The municipal board successfully advocated for enabling legislation to authorize them to offer dental coverage to retired members. As a result, the board will be offering two levels of dental plans to existing and future retirees effective March 1, 2010.

- The municipal board was able to make a third deposit into the Retiree Health Savings (RHS) accounts in February of 2009. The RHS accounts were established in July of 2007 and have been a tremendous help to many retirees by providing reimbursement for health care expenses and insurance premiums after retirement.

The Boards of Trustees

The boards of trustees are statutorily charged with establishing rules and regulations for the administration of their systems and for the transaction of their business. The boards delegate the day-to-day administration of the plans to the Retirement Division staff, utilizing the governing statutes and board-established rules and policies as guidelines. If questions arise, or if a member or retiree does not agree with a decision made by staff, they may appeal to their board for reconsideration.

The Attorney General's Office provides legal counsel to the boards when necessary. The boards also are charged with approving regular retirement applications, disability retirement applications, and withdrawals from membership. Each board of trustees acts as a fiduciary of the funds held on behalf of its members and retirees. The boards are required to keep a record of their proceedings, which are open to the public. Each board designates an actuary to make an annual valuation of the assets and liabilities of the funds of the system. Based on the actuarial recommendation, the State and teachers' boards advise the Governor on the annual amount of State contribution that should be appropriated for the next fiscal year to achieve and preserve the financial integrity of the funds.

Below is the current membership of the three boards of trustees. State Treasurer Jeb Spaulding is an ex officio member of all three boards.

Board Changes in 2009

In July of 2008, VMERS board member David Lewis retired and therefore could not run for re-election when his term expired in June of 2009. An election was held and his position as employer representative was filled by Amy Douglas, Town Clerk of Shoreham.

In the fall of 2008, Joe Mackey, active member representative on the teachers' board, was appointed to serve the remaining term of Jay Kaplan, who passed away in August of 2008. Mr. Mackey's position remained vacant until an election was held in the early summer of 2009. The results of the election established Tom McConnell as the active member representative on the teachers' board, serving a four-year term that began on July 1, 2009.

Warren Whitney, former Chair of the Vermont State Retirement Board, retired at the end of 2009 and as a result resigned his position as VSEA active employee representative on the board. David Herlihy, former Commissioner of Human Resources, was replaced by Caroline Earle, who was appointed Commissioner of Human Resources in the fall of 2009.

Current Membership of the Three Boards of Trustees

Vermont State Employees' Retirement System

Kevin Gaffney, Vice Chair, VSEA
Jeb Spaulding, State Treasurer
James Reardon, Commissioner
Dept. of Finance & Management
Caroline Earle, Commissioner
Dept. of Human Resources
Richard Johannesen, Governor's Appointee
Robert Hooper,VSEA
Paul White, VSEA
Roger Dumas, VRSEA
Joe Healy, Alternate-VRSEA

Vermont State Teachers' Retirement System

Jon Harris, Chair, Active Teachers
Joe Mackey, Vice Chair, Retired Teachers' Association
Jeb Spaulding, State Treasurer
Tom McConnell, Active Teachers
Thomas Candon, Banking, Insurance, Securities & Health Care Admin.
Vaughn Altemus, Department of Education

Vermont Municipal Employees' Retirement System

Steve Jeffrey, Chair, Employee Representative
Jeb Spaulding, State Treasurer
Stephen Rauh, Governor's Delegate
Peter Amons, Employee Representative
Amy Douglas, Employee Representative

Retirement Division Operations

Overview

The vast majority of State employees, teachers, and municipal employees participate in a defined benefit pension plan. Under such a plan, the employee upon retirement receives a monthly benefit, based on years of employment and salary history. As economic conditions steadily worsened in 2009, the division was challenged to respond to numerous inquiries from retirees and employees about the security of their retirement benefits. The division continues efforts to communicate with members about the security of their pensions.

The largest expenditure for all three defined benefit plans is the retirement benefit. During fiscal year 2009, the three retirement systems paid out more than $170 million in monthly benefit payments. As noted in the appendices, page 52, the benefit payout number continues to rise as more employees retire and as retirees live longer. This will put a continued burden on the systems and increases the

Retirement Operations
(802) 828-2305
(800) 642-3191 (toll-free in Vermont)

Michael Clasen, Retirement Operations Director

Cynthia Webster, Retirement Policy & Outreach Director

Laurie Lanphear, Chief Retirement Specialist

Monica Chiren, Retirement Customer Service Representative

Alice Cloud, Program Technician I

Nancy Dimick, Retirement Specialist I

Tina Kawecki, Retirement Specialist I

Kathleen Kretzer, Retirement Specialist I

Wendy Lee, Program Technician II

Jennifer Lilley, Financial Administrator II

Katherine McSorley, Program Technician II

Jaime Meredith, Program Technician I

Marge Sweeney, Retirement Project Manager

Cheryl Taylor, Program Technician I

ACCOMPLISHMENTS IN 2009

- **The Retirement Division staff conducted 1,196 individual counseling sessions during fiscal year 2009, a 5 percent increase over the prior year. It is noteworthy to point out that the staff conducted more counseling appointments in 2009 than in 2008, while at the same time devoting significant time to testing the new VPAS pension administration system.**

- **The staff calculated approximately 8,000 retirement estimates for prospective retirees, a 25 per cent increase over 2008, and conducted 90 member informational sessions across the state with 1,623 individuals in attendance.**

- **Legislation passed in June 2009 offered a retirement incentive to retirement-eligible State employees as a way to reduce the State payroll and help prevent additional employee layoffs. The incentive included a cash payment, as well as a seven-year guarantee for the current 80 percent subsidy for health insurance. The Retirement Division identified nearly 1,000 eligible employees, of which 337 submitted applications. There were 243 employees that followed through with the application process, and 168 employees that retired effective September 1, 2009. The remaining 75 employees were granted extensions, as permitted by law, to retire between October 2009 and March 2010. Given the condensed time frame, and the fact that July and August are typically the busiest months of the year for the division, the staff is to be commended for managing the incentive program in a timely and efficient manner.**

- **Participation in the 403(b) Investment Program for public school districts continued to grow in 2009. There are 25 supervisory unions that have adopted the program. As of September, 2009, 1,139 school employees were participating in the program and assets had grown to $6.54 million.**

Retirement Division Performance Indicators

Activity	2009	2008	2007	2006	2005	2004	Percent Change 2004 - 2009	Percent Change 2008 - 2009
Estimates	7,999	6,377	8,213	8,672	7,031	4,700	70%	25%
Individual Counseling	1,196	1,136	1,173	1,050	1,216	1,070	12%	5%
Retirements	907	867	788	785	716	655	38%	5%
Withdrawals	937	945	1,507	1,485	2,816	3,072	-69%	-1%
Deaths	316	368	333	278	279	265	19%	-14%
Seminars	90	61	88	51	53	57	58%	48%
Seminar Attendance	1,623	1,285	1,881	1,381	1,386	1,749	-7%	26%

need to meet annual funding requirements. In addition, both the Vermont State Employees' Retirement System (VSERS) and the Vermont State Teachers' Retirement System (VSTRS) have traditionally offered health insurance to their members by picking up a large portion of the premium – 80 percent for retired teachers and 80 percent for retired State employees and their dependents. In fiscal year 2009, these health care expenses for the two retirement systems totaled more than $34.3 million. The Vermont Municipal Employees' Retirement System (VMERS) does not offer a health insurance plan. In an effort to provide some health care assistance to members without undue burden to local municipalities, the VMERS board established a new health retirement savings plan in 2008 (see update page 17).

UPDATES

Serving Members' Needs

The primary function of the Retirement Division staff is to serve the needs of the active contributing members and retired members receiving benefit payments. On the active member side, the Retirement Division oversees enrollments, transfers, refunds, processing of employee and employer contributions, and adjustments to members' accounts. On the retiree side, the division oversees the

Day-to-day administration of the retirement systems is provided by the Treasurer's Office. The Retirement Division staff works with all active contributing members and retired members receiving benefit payments.

issuance of payroll, changes to dependents, adjustments to payments, and replacement checks. Other responsibilities include employee re-instatements, calculation of buy-backs and refunds, disability retirements, and determination of survivor benefits. The division manages an extremely high volume of inquiries by phone, e-mail, and face-to-face appointments. The division's accountant maintains all retiree data and ensures the timely processing of approximately 12,000 pension payments each month. The table above provides an update of division activities.

Retirement Re-engineering Project

Retirement Division staff spent the last three years working on the development and implementation of a new computer system, referred to as VPAS (Vermont Pension Administration System). In many cases, the staff devoted considerable time to the VPAS project while still managing to complete the work associated with their ongoing "day jobs." When fully operational, VPAS will replace the division's 30-year-old legacy computer system. The VPAS project is structured into three phases: imaging phase; retiree benefit payment phase; and the active member salary, contributions, and service credit phase. The imaging

HISTORICAL OVERVIEW & UPDATES

In accordance with State statutes, each retirement system is administered by a board of trustees. (See Vermont Retirement Systems section in this report.) The boards administer the State's three defined benefit pension plans and two defined contribution plans, with day-to-day administration provided by the Treasurer's Office. The Vermont State Employees' Retirement System (VSERS) is a single-employer public employee defined benefit retirement system that covers substantially all general State employees and State Police. The Vermont State Teachers' Retirement System (VSTRS) covers nearly all public day school and nonsectarian private high school teachers and administrators, as well as teachers in schools and teacher training institutions within and supported by the State that are controlled by the State Board of Education. The Vermont Municipal Employees' Retirement System (VMERS) is a multiple-employer public employees' retirement system. Employer contributions are made by the participating municipalities. It is designed for school districts and other municipal employees that work on a regular basis and also includes employees of museums and libraries, if at least half of that institution's operating expenses are met by municipal funds.

The State established an optional defined contribution plan for exempt State employees effective January 1, 1999. Although the division has contracted with a third-party administrator (Fidelity Investments) to handle

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the investment options and day-to-day bookkeeping responsibilities, the Treasurer's Office is responsible for providing new hires with information, counseling, and comparisons of projected benefits under both plans. Staff members process all transfers between the plans, and receive and transmit all contributions on behalf of the defined contribution members.

The Retirement Division also administers a deferred compensation (457) program for State and municipal employees and has recently expanded to teachers.

There also is a single depository investment account (SDIA)--a tax-sheltered account funded through employee transfers to a non-contributory system for State employees and teachers. This is a closed fund with no new additional contributions. The SDIA funds are not available to the members until they retire or terminate employment. As of June 30, 2009, there were 2,120 SDIA members, with net assets of $79,699,986. Great-West Retirement System provides third-party administration for these services.

The office administers a Retiree Health Savings plan for VMERS members. While health insurance is not available to retired municipal members, this plan provides a vehicle to set aside limited funds to reimburse retirees for medical expenses.

The State Employees' Post-employment Benefit Pension Trust Fund (an OPEB Trust Fund) was established in fiscal year 2007 as an irrevocable trust fund for the purpose of accumulating and providing reserves to support VSERS retiree post-employment benefits. While additional State appropriations may be made to this fund, contributions to date include medical subsidy reimbursements from the federal government for the Medicare D program and contributions to pay health care premiums for current retirees. During fiscal year 2009, the State contributed $19.9 million to this fund. The fund had total assets of $5,748,582 as of June 30, 2009.

phase has substantially been completed. The retirement benefit payment phase became operational beginning with the November 2009 pension payroll. Most of the changes were internal and allowed for more efficient and faster processing of new retirements and changes to existing retiree accounts. The VPAS also houses all of the data in one system that is backed up on a daily basis. The current plan is to begin rolling out the active member functionality in phases, to be completed by the end of fiscal year 2010. This phase will also house all data in the VPAS and allow for automation of a number of different business processes such as benefit estimate calculations and annual benefit statement production. Future enhancements to VPAS include a web-based member self-service feature that will allow active employees, as well as retirees, the ability to review their accounts on-line.

With the implementation of VPAS, every aspect of the daily business of the division will be impacted. This solution will provide the State of Vermont with a stable, state-of-the-industry, fully-integrated pension administration solution that will allow the division to operate its business more efficiently and effectively. The new system also will provide an infrastructure that lends itself to changing technology and provide a broader framework for administering the system. Additionally, customers' needs for increased access to services and more timely information will be met.

Pension Funding

The State appropriates funding for pension costs associated with the VSERS and VSTRS plans. Currently, the State's contribution to each system is based on percentage rates of each member's annual earnable compensation. These rates include a "normal contribution" rate and an "accrued liability contribution" rate and are calculated based upon the liabilities of each system as determined by actuarial valuations. The State was statutorily responsible for contributions to the VMERS' pension accumulation fund, prior to July 1, 1987. However, since July 1, 1987, all payments to the system's pension accumulation fund are supported entirely by employer (municipal) and employee contributions. Employers make quarterly payments into the pension accumulation fund. These payments are percentages of annual earnable compensation for each membership group and consist of a "normal" and an "accrued liability" portion. The percentage rates of such contributions are fixed on the basis of the liabilities of the system pursuant to actuarial valuations.

The State of Vermont's contribution to each system is based on percentage rates of each member's annual earnable compensation.

Actuarial Valuation - Methods and Assumptions

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Actuarially determined amounts are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The actuarial method for both the VSTRS and the VSERS plans is set by State statute. Through fiscal year 2005, the method used was entry age normal (EAN) with frozen initial liability (FIL). The legislature enacted a statute change revising the method to entry age normal without FIL for the actuarial valuation for the year ending June 30, 2006. This change in method effectively reset the starting balance. Under the previous method, set by State statute, the unfunded liability was frozen at 1988 levels. Any impact of underfunding subsequent to the "freezing" of the liability in 1988 falls to normal cost, instead of being added to the unfunded liability as in more conventional funding methods. In the case of VSERS, changing the method did not have a significant impact because the contributions

Comparative Membership Information--Vermont Retirement System

Vermont State Employees' Retirement System			
	June 30, 2009	June 30, 2008	Percent Change
Active Members			
Vested	5,752	5,753	-0.02%
Not Vested	2,343	2,689	-12.87%
Total Active Members	8,095	8,442	-4.11%
Average Age	46.95	46.55	0.86%
Average Service	12.65	12.27	3.10%
Average Compensation	$ 49,971	$ 47,967	4.18%
Retired Members and Beneficiaries			
Number	4,797	4,555	5.31%
Annual Retirement Allowances	$ 73,179,785	$ 65,701,435	11.38%
Inactive Members	939	900	4.33%
Terminated Vested Members	798	789	1.14%

State Teachers' Retirement System of Vermont			
	June 30, 2009	June 30, 2008	Percent Change
Active Members			
Vested	8,076	7,902	2.20%
Not Vested	2,723	2,783	-2.16%
Total Active Members	10,799	10,685	1.07%
Average Age	47.07	$ 46.89	0.38%
Average Service	13.77	13.62	1.10%
Average Compensation	$ 52,004	$ 50,146	3.71%
Retired Members and Beneficiaries			
Number	5,910	5,555	6.39%
Annual Retirement Allowances	$ 91,393,401	$ 82,480,807	10.81%
Inactive Members	2,655	2,929	-9.35%
Terminated Vested Members	721	705	2.27%

Vermont Municipal Employees' Retirement System			
	June 30, 2009	June 30, 2008	Percent Change
Active Members			
Vested	3,585	3,424	4.70%
Not Vested	2,948	2,995	-1.57%
Total Active Members	6,533	6,419	1.78%
Average Age	47.80	47.27	1.12%
Average Service	7.34	7.02	4.56%
Average Compensation	$ 29,316	$ 27,402	6.98%
Retired Members and Beneficiaries			
Number	1,538	1,447	6.29%
Annual Retirement Allowances	$ 10,149,148	$ 9,015,096	12.58%
Inactive Members	2,015	2,035	-0.98%
Terminated Vested Members	554	486	13.99%

received closely mirrored the actuarial requirements. However, the 30-year period for amortization of the unfunded actuarial accrued liability was restarted effective July 1, 2008.

Actuarial Accrued Liability Determinations

In the case of VSERS, the actuarial accrued liability for current retired members, terminated vested members, and beneficiaries is $760,453,336. The actuarial accrued liability for current active and inactive members is $783,690,730. Together, the total actuarial accrued liability comes to $1,544,144,066. The actuarial value of assets is $1,217,637,578, resulting in an unfunded accrued liability of $326,506,488.

Under legislation enacted in fiscal year 2008, VSERS benefits were modified in three respects for members hired on or after July 1, 2008. First, the maximum benefit payable was increased from 50 percent to 60 percent of the average final compensation (AFC). Second, the eligibility condition for an unreduced benefit changed from the attainment of age 62 or 30 years of service to a "rule of 87."

The "rule of 87" required that an employee attain that number through a combination of years of service and age.

Third, for members not eligible for an unreduced benefit, the reduction for early retirement changed from a uniform 6 percent per year to one determined on a service-based schedule. Due to the relatively small number of participants affected by the hire date incorporated in these changes, the actuary reports a minimal impact on the normal cost and accrued liability. The remaining significant provision of the same legislation makes changes to retiree cost of living (COLA) adjustments. The annual COLA applicable to the benefits of Group F members retiring after July 1, 2008, rose from 50 percent of the annual increase of the Consumer Price Index (CPI) to 100 percent of the annual increase in the CPI index, up to a ceiling of 5 percent effective January 1, 2014. Only current Group F members who were actively contributing into the system on June 30, 2008 and retire on or after July 1, 2008, will be eligible for the enhanced COLA in 2014. Group F members who terminated service or transferred to another group plan prior to June 30, 2008, are not eligible for the new COLA unless they return to active Group F service after July 1, 2008, and prior to retirement. The total net actuarial loss for the VSERS system from June 30, 2008, to June 30, 2009, is $243,194,030. Investment losses during the recent economic cycle accounted for almost all of the change, $242,482,443. Other significant factors impacting the actuarial loss were COLA experience and new entrants with prior service - with offsetting gains in mortality experience, retirement and termination experience, and the reimbursement of expenses.

In the case of VSTRS, the actuarial accrued liability for current retired members, terminated vested members, and beneficiaries is $972,834,725. The actuarial accrued liability for current active and inactive members is $1,129,003,118. Together, the total actuarial accrued liability is $2,101,837,843. The actuarial value of assets is $1,374,079,337, resulting in an unfunded accrued liability of $727,758,506. There were no changes in the benefit provisions since the prior valuation. Benefit modifications were made in both 2008 and 2009. Actuarial assumptions remain the same as in the previous valuation. The total net actuarial loss for the VSTRS from June 30, 2008, to June 30, 2009, is $341,414,763. Investment experience accounted for $312,726,392. Other significant factors increasing the actuarial loss were expenses other than investment expenses, termination experience, COLA experience, and new entrants with prior service. Retirement and mortality experience partially offset this, as well as other factors.

FUNDING PROGRESS OF THE RETIREMENT SYSTEMS

VSERS

Year Ending 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)
2009	$1,217,638	$1,544,144	$326,506	78.9%	$404,516	80.7%
2008	1,377,101	1,464,202	87,100	94.1%	404,938	21.5%
2007	1,318,687	1,307,643	(11,044)	100.8%	386,917	-2.9%
2006	1,223,323	1,232,367	9,044	99.3%	369,310	2.5%
2005	1,148,908	1,174,796	25,889	97.8%	349,258	7.4%
2004	1,081,359	1,107,634	26,275	97.6%	336,615	7.8%
2003	1,025,469	1,052,004	26,535	97.5%	319,855	8.3%
2002	990,450	1,017,129	26,679	97.4%	300,994	8.9%
2001	954,821	1,026,993	72,172	93.0%	278,507	25.9%
2000	895,151	967,064	71,913	92.6%	266,519	27.0%
1999	804,970	876,412	71,442	91.9%	238,281	30.0%
1998	733,716	804,501	70,785	91.2%	235,956	30.0%
1997	639,128	753,883	114,755	84.8%	227,000	50.6%
1996	560,659	664,173	103,514	84.4%	226,792	45.6%
1995	480,049	679,427	199,378	70.7%	225,089	88.6%

VSTRS

Year Ending 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)
2009	$1,374,079	$2,101,838	$727,759	65.4%	$561,588	129.6%
2008	1,605,462	1,984,967	379,505	80.9%	535,807	70.8%
2007	1,541,860	1,816,650	274,790	84.9%	515,573	53.3%
2006	1,427,393	1,686,502	259,108	84.6%	499,044	51.9%
2005	1,354,006	1,492,150	138,144	90.7%	468,858	29.5%
2004	1,284,833	1,424,661	139,829	90.2%	453,517	30.8%
2003	1,218,001	1,358,822	140,821	89.6%	437,239	32.2%
2002	1,169,294	1,307,202	137,908	89.5%	418,904	32.9%
2001	1,116,846	1,254,341	137,496	89.0%	403,258	34.1%
2000	1,037,466	1,174,087	136,621	88.4%	387,999	35.2%
1999	931,056	1,065,754	134,698	87.4%	372,299	36.2%
1998	821,977	955,694	133,717	86.0%	357,899	37.4%
1997	717,396	849,179	131,783	84.5%	364,695	36.1%
1996	570,776	700,377	129,601	81.5%	355,895	36.4%
1995	520,850	648,052	127,202	80.4%	346,975	36.7%

VMERS

Year Ended 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)**
2009	$331,407	$366,973	$ 35,566	90.3%	$191,521	18.6%
2008	348,740	343,685	(5,055)	101.5%	175,894	-2.9%
2007	325,774	309,853	(15,921)	105.1%	162,321	-9.8%
2006	288,347	276,552	(11,795)	104.3%	148,815	-7.9%
2005	259,076	248,140	(10,936)	104.4%	146,190	-7.5%
2004	232,890	225,092	(7,798)	103.5%	135,351	-5.8%
2003	222,854	218,533	(4,321)	102.0%	126,216	-3.4%
2002	193,278	176,109	(17,169)	109.7%	106,986	-16.0%
2001	177,928	158,786	(19,142)	112.1%	101,873	-18.8%
2000	161,900	138,697	(23,203)	116.7%	87,147	-26.6%
1999	137,454	114,481	(22,973)	124.6%	70,808	- 32.4%
1998	113,678	102,005	(11,673)	111.4%	87,328	- 17.3%
1997	96,196	85,686	(10,510)	112.3%	70,800	-14.8%
1996	81,396	73,401	(7,995)	110.9%	68,700	-11.6%

The actuary has estimated the change in the unfunded actuarial accrued liability between June 30, 2008, and June 30, 2009, as follows:

	VSERS	VSTRS
Unfunded actuarial accrued liability, June 30, 2008	$ 87,100,468	$ 379,505,069
Normal cost	44,574,324	35,690,059
Contribution paid	(48,324,859)	(60,652,640)
Interest on unfunded liability, normal cost and contribution	8,909,271	31,801,254
Actuarial gains and losses/experience	243,194,030	341,414,764
Assumption changes	-	-
Changes to benefits/system provisions	(8,946,746)	-
Unfunded actuarial accrued liability, June 30, 2009	$ 326,506,488	$ 727,758,506

Defined Contribution Plan

State Defined Contribution Plan: Established in 1999, the State's defined contribution plan had 589 participants and net assets of $32,737,781 as of June 30, 2009. Under the defined contribution plan, which is modeled after private sector 401(k) plans, employees contribute 2.85 percent of their annual salary to their individual accounts. The State makes a fixed contribution of 7 percent to each employee's account. Employees are responsible for making all investment decisions. Fund line-ups are negotiated by the Treasurer's Office and included in the contract with plan administrator, Fidelity Investment. At retirement or termination, employees receive the amount of contributions in their accounts, plus investment earnings. The defined contribution plan provides portability for an increasingly mobile workforce. The plan offers 11 mutual funds in equity, balanced, and fixed income asset classes, and age-based "life-cycle" funds that rebalance a multi-asset class portfolio of mutual funds appropriate to the age of the plan participant. Options include a stable value fund that has insured principal value; an intermediate term bond fund; a balanced fund of stocks and bonds, large-, mid- and small-capitalization domestic equity funds; and an international equity fund. The plan is self-directed with respect to investment selection, meaning that participants elect investment options consistent with their risk and reward preferences along with the timing of their need to access funds. In calendar 2007, the State modified and renewed its contract with the plan's administrator following a lengthy RFP (Request for Proposals) process. The new contract provides for increased flexibility to change investment options when warranted, and the plan continues to be provided to participants without costs above the fund investments' intrinsic expense ratios.

Municipal Defined Contribution Plan: The Vermont Municipal Employees' Retirement System was given statutory authority in 1999 to approve a defined contribution plan for its members. The board implemented a defined contribution plan on July 1, 2000. The plan provides the employer municipality with the first option of deciding whether or not to offer a defined contribution plan to its employees. Once a municipality elects to offer the plan to all eligible employees or to specific employment groups, an individual employee has the choice to remain with the defined benefit plan or transfer to the new defined contribution plan. New employees of municipalities offering both a defined contribution plan and a defined benefit plan have a choice of either plan. As of June, 30, 2009, there were 70 contributing municipalities with 594 participants and net assets of $11,656,033.

Deferred Compensation: 457 & 403(b) Plans

The deferred compensation program has been available since 1979 as a savings option for State employees, municipal employees, employees of agencies such as VEDA and VHFA, and members of the General Assembly. The program is administered by Great-West Retirement Services. Since the deferred compensation plan qualifies as a Section 457 plan under the Internal Revenue Code, the portion of salary that is deferred is not taxed at the time of deferral. On June 30, 2009, the plan had 6,578 participants. Total assets in the plan were valued at $213.12 million. Participating employees made contributions in the amount of $17.29 million to the plan during fiscal year 2009.

A 403 (b) Investment Program for public school districts was implemented on January 1, 2009. The program allows school employees to deduct money from their wages on a tax-deferred basis that may be invested in a variety of mutual funds during the employee's working years. The 403(b) contributions reduce taxable wages during employment, and the money accumulates tax-free until the funds are withdrawn after retirement. At that time, all of the money is taxable as regular income to the participant. The program is administered by Great-West Retirement Service. The initial enrollment endeavor resulted in 25 supervisory unions adopting the 403(b) program. During the first quarter of activity, 884 participants elected to participate, and plan assets totaled $1.69 million by the end of March, 2009. By the end of September, 2009, the participant count had grown to 1,139 and the assets had grown to $6.54 million.

Retiree Health Savings Plan Update

In July of 2007, the Vermont Municipal Employees' Retirement Systems (VMERS) Board of Trustees created a Retiree Health Savings (RHS) Plan administered by ICMA-RC. The RHS Plan was designed to provide members and retirees with funds which could be used on a tax-free basis to reimburse medical expenses and insurance premiums incurred and paid for after retirement. The VMERS board determined that all active and retired members that had paid contributions into the VMERS for a minimum of five years as of June 30, 2006, would be eligible to participate in the RHS plan. On July 2, 2007, the board distributed more than $5 million into 3,545 active member accounts and 1,159 retired member accounts.

The RHS Plan provides members and retirees with funds that can be used on a tax-free basis to reimburse medical expenses and insurance premiums incurred and paid for after retirement.

The RHS Plan money is invested into individual, age appropriate Milestone accounts at ICMA-RC. Active members cannot use the RHS Plan funds until they begin to draw their VMERS pension benefits. Retired members may use the money at any time for medical and insurance expenses incurred and paid after July 1, 2007. A second contribution of $3.5 million was made into the RHS accounts on August 1, 2008, and a third contribution of approximately $2.5 million was made in February of 2009, for a total combined deposit of $11 million. From January 1, 2008, through December 31, 2009, more than $1.15 million was disbursed to retired members seeking reimbursement for their medical and premium expenses. Comments from retirees who have used their RHS money continue to be very positive and appreciative. Many feel it makes a very real difference in being able to pay for their medical care, and even in deciding whether to go to their physician or not.

UPDATE: Single Deposit Investment Account

The Single Deposit Investment Account (SDIA), a non-contributory defined contribution plan reported in the Pension Trust Funds, was established according to the provisions of Public Act 41 of the 1981 Session. The SDIA was intended to provide an investment vehicle in which to deposit contributions made by members of the State and Teachers' contributory retirement systems who voluntarily elected to transfer to the newly established non-contributory retirement systems. In addition to the initial deposits made into the SDIA in 1981, there were three subsequent opportunities (in 1984, 1987, and 1990) for contributory members to transfer to the non-contributory plans and invest their accumulated contributions and interest in the SDIA. No new monies have been invested in the SDIA since 1990. As of June 30, 2009, there were 2,120 SDIA members, with net assets of $79,699,986. Administrative services for the SDIA are provided by Great-West Retirement Services. Great-West administers the day-to-day activities of the SDIA, including maintaining all demographic and beneficiary information, processing all requests for withdrawals and minimum distributions, and maintaining member account value information.

Other Post-Employment Benefits (OPEB): Health Care

Vermont State Employees' Retirement System

Employees retiring directly from active State service for any reason, may carry whatever coverage is in effect at that time into retirement for themselves and their dependents. During the lifetime of the retiree, currently only 20 percent of the cost of the premium is paid by the retiree. If the retiree chooses the joint and survivor pension option, and predeceases his or her spouse, the medical benefits may also continue for the spouse, along with the pension. However, generally the surviving spouse must pay 100 percent of the cost of the premium. In addition, once retirees become eligible for Medicare coverage (at age 65) it is mandatory that they enroll in both Medicare Part A and Part B, making Medicare the primary insurer. If an employee, other than a Group C member, does not retire directly from State service, he or she is not eligible to participate in the State's medical insurance plan. Group C members who terminate with 20 or more years of service, but are not yet 50, may pick up the medical coverage at the time they begin retirement benefits. If the insurance is terminated at any time after retirement, coverage will not be able to be obtained again at a later date. Based on legislation enacted during fiscal year 2008, Group F employees hired after July 1, 2008, will receive a tiered retiree health care reimbursement based on years of service. This group also may recapture (access) subsidized health insurance at 80 percent upon initiation of retirement benefits in a manner comparable to regular retirements. This applies even if the employee terminated prior to his or her early retirement date, providing the member has 20 years of service. At the time this initiative was passed it was projected to save approximately $265 million over 30 years on a pay-as-you-go basis.

As of June 30, 2009, 3,571 retirees were enrolled in the medical plan in the single, spouse, and family plan options. The retirees contributed $5.1 million in premiums and incurred $26.7 million in claims expenses for the fiscal year ending June 30, 2009. The State's fiscal year 2009 contributions to the VSERS included, on a pay-as-you-go basis, $18.1 million for the State's share of the cost of the premiums. The VSERS paid S17.9 million in premiums, on a pay-as-you-go basis, to the Medical Insurance Fund for this benefit in fiscal year 2009.

State Teachers' Retirement System

VSTRS retirees participate in multi-employer health coverage plans operated by the Vermont Education Health Initiative (VEHI) which is managed jointly by the Vermont School Boards Insurance Trust and the Vermont-National Education Association. VEHI partners with Blue Cross Blue Shield to provide health insurance to retired and active teachers. VSTRS members have access to three plans in retirement that are identical to those offered to active teachers in Vermont's public school systems. Members may pick up medical coverage under one of the plans for themselves and all eligible dependents at the time of retirement, or anytime thereafter during semi-annual open enrollment periods. The system pays 80 percent of the retiree's premium only, for members with a minimum of 10 years of creditable service. Payment is based on the cost of the "standard plan" as defined by statute. The retiree pays the full cost of the premium for all covered dependents.

As of June 30, 2009, 3,932 retirees were enrolled in the single, spouse, and family medical plan options. In the 2009 fiscal year, retirees contributed $10.96 million in premiums and the system paid $16.7 million in premiums and $16.4 million, on a pay-as-you-go basis. Once retirees becomes eligible for Medicare coverage (at age 65), it is mandatory that they enroll in both Medicare Part A and Part B. Medicare becomes the primary insurer and the Teachers' medical plans become the secondary carrier. Two of the plans offered become "carve-out" plans to coordinate with Medicare, and one of the plans is replaced with a true Medicare supplemental plan.

OPEB Funding Status

Starting in fiscal year 2008, the Government Accounting Standards Board required the disclosure of OPEBs in the State's financial reports. OPEB refers to any post-employment benefit other than pensions, although medical is the most significant component. Currently, the State does not prefund its OPEB benefits, with the exception of a small portion of Medicare D reimbursements from the State employees' system. The State system is 0.7 percent funded and the teachers' system is 0 percent.

Vermont OPEB Liabilities

STATE EMPLOYEES	8.25% (Pre-funding Assumed)	4.25% (Partial Funding Basis)
Unfunded Liability:	$448.5 million	$775 million
ARC for FY 2010:	$37.6 million	$58 million
Pay-As-You-Go Applied to ARC:	$22 million	$22 million
TEACHERS		4.0% (No Pre-funding)
Unfunded Liability:	$431.8 million	$872.2 million
ARC for FY 2010:	$32.2 million	$59 million

The State's annual OPEB cost is calculated based on the annual required contribution of the employer (ARC). That contribution is actuarially determined in accordance with the parameters of the Government Accounting Standards Board (GASB) Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal costs each year and amortize any unfunded actuarial liabilities over a period not to exceed 30 years.

In the case of VSERS, health care expenses are included in an administrative budget appropriated and transferred to a system's pension fund which pays the health care premiums through an established sub-fund. These are expressly funded, separate from the pension actuarial contribution. In the case of VSTRS, the health care expenses are also paid through a sub-fund of the pension fund, but are not explicitly budgeted and so are not included in the net OPEB obligation (NOO) calculation. Health care expenses are reflected as part of the pension fund. The funding progress for the two systems is as follows:

Actuarial Valuation Date 6/30	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)
VSERS						
2009	$5,749	$812,987	$807,238	0.7%	$426,827	189.1%
VSTRS						
2009	$0	$872,236	$872,236	0.0%	$561,588	155.3%

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Actuarially determined amounts are subject to continual revision, as actual results are compared with past expectations and new estimates are made about the future.

OPEB Actuarial Valuation: Methods and Assumptions

The actuarial accrued liability for OPEB obligations earned through June 30, 2009, is $780.7 million, with an unfunded actuarial liability of $775 million. The plan participant count was increased from 11,815 to 13,468. This increase in liability was partially offset by adjustments to the estimated per capita claims due and the allocation of expected claims between pre- and post-65-year-old participants. The results also incorporate a change to the plan provisions to reflect the fact that Group F employees hired after July 1, 2008, will receive a tiered retiree health care premium reimbursement based on completed years of service, as previously noted. All assumptions, including health care inflation rates, separation, coverage, and coverage participation rates, were the same as in the previous valuation with the exception of the discount rate. An OPEB trust has been established for VSERS and

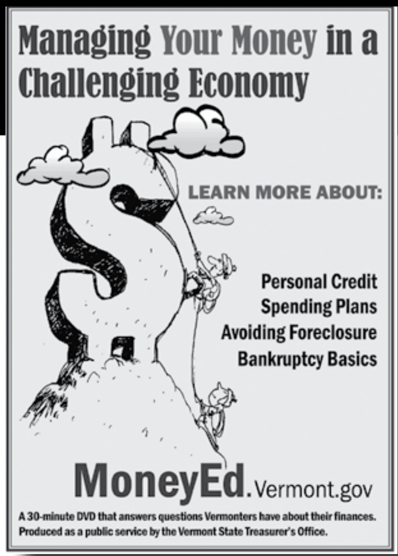
The annual required contribution of the State for OPEBs is calculated to commence at $37.6 million for fiscal year 2010 and is projected to increase to $154.6 million for fiscal year 2039.

is funded in part as required by statute through the deposit of Medicare-D subsidies received for State employees' prescription programs. Therefore, the VSERS reflects a "blended rate" reflecting some level of prefunding, resulting in an assumed discount of 4.25 percent, instead of the pay-as-you-go liability calculated at 4 percent. To fully amortize this liability over a 30-year period (utilizing an amortization with installments increasing at a rate of 5 percent per year) would require an ARC commencing at $58 million for fiscal year 2010 and projected to increase to $267.6 million in fiscal year 2040. If, however, pre-funding is assumed, the actuarial accrued liability is reduced to $427.2 million with an unfunded actuarial liability of $454.2 million. The ARC is calculated to commence at $37.6 million for fiscal year 2010 and projected to increase to $154.6 million for fiscal year 2039. Upon retirement of the unfunded accrued liability, the projected normal cost in fiscal year 2040 on a pre-funding basis is $65.2 million. The fiscal year 2010 State budget funds the current year expected benefit payments of approximately $21.1 million, which is less than the ARC applicable under either funding basis.

An OPEB trust has not been created for VSTRS and no pre-funding has been made. An OPEB valuation and an experience study was completed for VSTRS. Demographic assumptions in the June 30, 2009, OPEB valuation are consistent with those used to value the system's pension benefits and do not reflect any changes from the previous OPEB valuation. There were no changes to plan provisions. An increase in the liability is due to an increase in the participant population from 15,194 to 15,576.The increase in liability was partially offset by the fact that here were no increases in health care premium costs for the past year. For VSTRS, assuming no prefunding, the actuarial accrued liability and the unfunded actuarial liability for OPEB obligations earned through June 30, 2009, is $872.2 million. To fully amortize this liability over a 30-year period (utilizing an amortization with installments increasing at a rate of 5 percent per year) would require an ARC commencing at $59 million for fiscal year 2010 and projected to increase to $266.2 million in fiscal year 2040. If, however, pre-funding is assumed, the actuarial accrued liability and the unfunded actuarial liability is reduced to $431.9 million. The ARC is calculated to commence at $32.2 million for fiscal year 2010 and is projected to increase to $132.5 million for fiscal year 2039. Upon retirement of the unfunded accrued liability, the projected normal cost in fiscal year 2040, on a pre-funding basis, is $45.6 million.

Vermont Retirement Systems -- Year Ended June 30, 2009
Summary of Operations

Category	Vermont State Retirement System	Vermont State Retirement System-OPEB	State Teachers' Retirement System	Municipal Employees' Retirement System
SOURCES OF FUNDS				
Employee Contributions	$ 25,134,235	0	20,937,686	9,557,973
Employer Contributions	$ 22,148,754	19,893,129	35,960,934	8,008,862
Other Income	$ 1,041,870	0	3,754,020	1,321,919
Investment Income (Reduction)	$ (242,976,381)	86,454	(307,382,559)	(56,937,342)
APPLICATION OF FUNDS				
Retirement Benefits	70,043,119	0	89,825,986	10,228,263
Refunds	1,403,995	0	1,420,776	1,223,465
Health/Life Insurance Expenses	0	17,894,518	16,421,176	0
Administrative Expenses	1,219,287	0	1,249,774	798,458
Other Expenses	477,966	0	606,434	588,899
Addition (Reduction) to Net Assets Held In Trust for Pension Benefits	$ (267,795,889)	$ 2,085,065	$ (356,254,065)	$ (50,887,673)



Financial Literacy

The Treasurer's Office implemented a MoneyEd initiative in 2009 to promote a better understanding of basic personal finance among Vermonters.

Financial Literacy
(802) 828-3706

Lisa Helme
Financial Literacy & Communications Director

Background

The Treasurer's Office continues its commitment to promoting, assessing, developing, and supporting efforts and programs to further financial literacy among Vermont citizens. Aided in 2009 by funds from the legislatively approved Financial Literacy Trust Fund, the Treasurer's Office introduced several new initiatives and began planning work for future financial education programs.

UPDATES

New Financial Education Tools Developed

The Treasurer's Office implemented a MoneyEd initiative in 2009 to promote a better understanding of basic personal financial topics among adult Vermonters. In early spring, the office began production on a 30-minute personal finance DVD that focused on the top questions Vermonters have about managing their household budgets in this time of economic change. The program features interviews with Vermont experts on four key areas: personal credit, budgeting, housing, and personal bankruptcy. In addition, short feature segments examined identity theft, consumer rights, saving for retirement, and qualifying for a home loan. The program aired on 23 Vermont public access stations the week of May 10 and was shown more than 100 times. The DVD also was sent to all public

ACCOMPLISHMENTS IN 2009

- **Produced and distributed 30-minute educational program titled "Managing Your Money in a Challenging Economy." The program aired on 23 Vermont public access stations and was distributed to all public libraries in the state.**
- **Organized and conducted first-ever Vermont Championship Reserve Cup Challenge for high school students. Held in partnership with the Federal Reserve Bank of Boston, the competition promotes student interest in and knowledge of personal finance, economics, and consumer affairs. Six high schools participated.**
- **Conducted statewide financial literacy poster contest for the second year in a row and attracted twice as many student entries as last year. Ten schools and 155 student entries were received for the competition. Vermont's elementary school poster winner went on to be recognized nationally as the second place winner for her division.**
- **Created and conducted financial readiness workshop for deploying Vermont National Guard troops and their families. Workshops were held at all Yellow Ribbon troop events throughout the state. More than 400 soldiers and family members participated in the workshop.**
- **Sponsored screenings of a new national documentary by FINRA on investment fraud at events in Burlington, Montpelier, Rutland, and St. Johnsbury. The events were in support of Save for Retirement week in October. The events attracted 112 participants.**

libraries in Vermont. A two-page resource guide was distributed with the DVD to guide Vermonters to resources they could access for questions related to the show's content. Vermonters may continue to view the program through a MoneyEd web page where program segments are available on line. This initiative was underwritten by funds contributed to the Financial Literacy Trust Fund.

The Treasurer's Office completed and distributed a new educational fact sheet on teaching kids about money. The two-sided handout relates information on financial concepts to share with children from toddlers to high school age children. Money exercises also are included and Vermonters are directed to additional on line resources for more activities. Through a special financial literacy section on the Treasurer's Office web site called "Just for Parents and Kids," Vermonters can access a variety of additional materials.

Financial Education for Youth

High school teams from throughout Vermont had their knowledge of economics and personal finance tested in the first-ever Vermont Championship Reserve Cup Challenge. After three rounds of vigorous questioning, Essex High School emerged as the champion. Second place was won by Windsor High School and the third place finisher was North Country Union High School. The State Treasurer's Office, in partnership with the Federal Reserve Bank of Boston, held the competition in May to select a state winner to represent Vermont in the fall at

The Essex High School team poses with the championship cup following the May 2009 competition.

"Events like this provide an added incentive for students to push their envelope of understanding and have a public opportunity to display their knowledge."

-- Essex High School Social Studies Teacher Charlie Burnett

the New England regional competition in Boston. The purpose of the competition is to promote student interest in and knowledge of personal finance, economics, and consumer affairs topics. For the past four years, the Federal Reserve Bank of Boston has sponsored the regional competition as part of its economic literacy program. Organizing the state competition gave the Treasurer's Office an opportunity to involve more high schools in this educational program. In addition to the schools placing in the championship, high school teams from Mill River Union High School, River Valley Technical Center, and Stafford Technical Center. Four-person student teams competed against each other in a quiz-show style contest that tested both individual and team knowledge (see side feature examples). In the regional competition, Essex High School tied for third place with schools from Connecticut, New Hampshire, and Rhode Island. Belmont High School, representing Massachusetts, won the event. In May 2010, another Vermont championship will be held to select a high school to represent the state in the next New England competition. This program was made possible by funds provided through the Financial Literacy Trust Fund.

Lindsay Appleton of Reading Elementary School won her grade category at the state level. Her poster went on to place nationally as the runner-up in the elementary school grade category.

Three "would-be" student millionaires were recognized for their poster artistry in April as they designed posters around the theme: "I'm going to be a millionaire because I…" State winners in three grade divisions were recognized as part of April as Financial Literacy for Youth month. The Treasurer's Office, Consumer Credit Counseling Service of New Hampshire and Vermont, and the Vermont Bankers Association sponsored the competition for the second year as a way to promote financial education for youth. The state-wide competition was part of the National Foundation for Credit Counseling's annual poster contest. In all, ten schools participated and 155 students entered the competition. The winner of the elementary division was Lindsay Appleton from Reading Elementary School.

Her poster also was recognized at the national level. Appleton's portrayal of a deer in a money belt in a sunny Vermont field with the caption, "I'm going to be a millionaire because I save my bucks," placed second nationally in the elementary division. The middle school division was won by Brittany Hoyt of Williston Central School. Jacob Alan Leete, of the River Bend Technical Center, won the high school division.

The poster above was used to promote four showing of a national documentary on investment fraud. Fraud experts say that the downturn in the market has made people more vulnerable to fraud as they strive to recoup their losses.

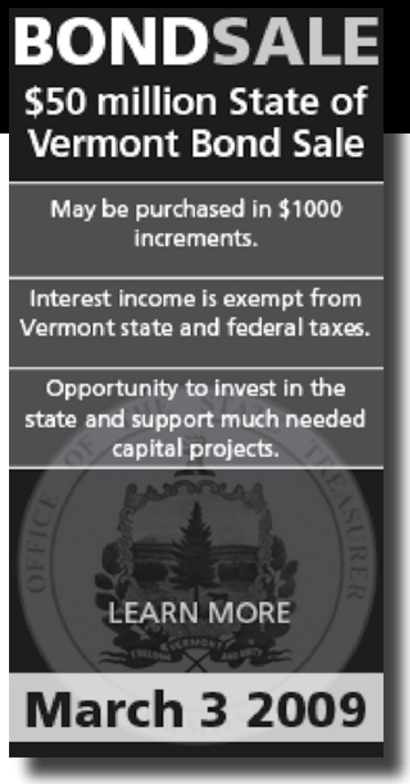
Adult Financial Literacy

The Treasurer's Office was pleased to support the Vermont National Guard by conducting a financial readiness workshop at all of the Yellow Ribbon briefing events held for the deploying troops and their families. In all, the National Guard conducted seven events at locations throughout the state prior to the troops deploying. The guard estimates more than a thousand soldiers attended the events, along with approximately 850 family members. The 45-minute financial readiness workshop covered three personal finance areas: organizing your finances, budgeting, and credit. The workshop incorporated segments from the MoneyEd DVD discussed earlier in this report along with personal instruction. The Treasurer's Office also obtained copies of the 2009 Consumer Action Handbook for each soldier's family. The 169-page handbook published by the U.S. Government covers dozens of topics including privacy protection and identity theft; smart home shopping; banking; credit; housing; insurance; investing; and filing a consumer complaint. There were 424 soldiers and family members who attended the workshop across all locations. In addition, the Treasurer's Office made available the unclaimed property database and encouraged soldiers and family members to look for property. More than a thousand searches were made. To provide ongoing support for the troops, the Treasurer's Office has made available a new section on its web site with information specially organized for deploying soldiers and family members. This program was underwritten by funds contributed to the Financial Literacy Trust Fund.

The guard estimates more than a thousand soldiers attended the Yellow Ribbon events, along with approximately 850 family members. The financial readiness workshop was attended by 424 soldiers and family members across all locations.

Each year, the Treasurer's Office looks for new information and services to offer during the "Save for Retirement Week" observance. This year, the Treasurer's Office partnered with the FINRA Investor Education Foundation to provide a free viewing of a new national documentary on investment fraud. Four events were held throughout the state and attracted 112 participants. Events were held in St. Johnsbury, Montpelier, Burlington, and Rutland. In addition to watching the 50-minute documentary, attendees could check for unclaimed property; receive information on State, teacher or municipal retirement plans; talk with a BISCHA fraud investigator; and receive general financial education materials.

The Treasurer's Office continues to offer the class, "Keeping the Gold in Your Golden Years." The class is a 90-minute workshop that teaches adults how to determine how much money they'll need in retirement, how to assess their current retirement savings resources, and implement a plan to ensure they will have adequate financial resources available to them in retirement. In calendar year 2009, seven workshops were conducted for 138 students. The majority of evaluations continue to rate the class as "very helpful."



Debt Management

Current Environment

The 2008-2009 worldwide financial crisis impacted the municipal bond markets to a degree not seen since the Great Depression, and not experienced by even the most senior banking professionals in their lifetimes. For periods of days and even weeks, municipal bond markets were closed to all but the highest quality issuers, and then only at significantly higher interest costs. The most notable impacts to date have been:

- By early 2009, the insolvency, merger, or departure from the market of six of the top ten municipal underwriting firms of 2007.

ACCOMPLISHMENTS IN 2009

- **In fiscal year 2009, the State Treasurer's Office issued $50,500,000 par amount of State of Vermont General Obligation Bonds, 2009 Series A. The bonds were sold through a negotiated offering senior managed by Citi and had an average life of 10.5 years and true interest cost of 3.82 percent. This very competitive interest rate was due in large measure to the State's very strong credit ratings.**

- **Vermont maintained its General Obligation (G.O.) Bond credit ratings of Aaa from Moody's Investors Service (Moody's), AA+ from Standard and Poor's Ratings Group (S&P) and AA+ from Fitch Ratings (Fitch), which are the highest ratings of all six New England states. As reported by Moody's, the State's critical debt ratios of "net tax supported debt per capita" and "net tax supported debt as a percent of personal income" also improved to rankings of 34th and 35th among the fifty states, respectively (50th is the best ranking).**

- **The Treasurer's Office, with the assistance of the Agency of Transportation, Legislative Joint Fiscal Office, and investment banks Citi and Morgan Stanley, prepared a transportation study entitled, "Bridges and Culverts Long-Term Assessment and Funding Options." In part due to this report's recommendations, the Legislature created a motor fuel transportation infrastructure assessment. The assessment provides revenues dedicated to paying the costs of rehabilitation, reconstruction or replacement of bridges, culverts, roads, airports, railroads and other transportation-related expenses that are critically important to the State's economy.**

- **The Capital Debt Affordability Advisory Committee (CDAAC) recommended increasing the State's annual bonding level to $71.825 million in fiscal year 2011, an increase of 2.7 percent from fiscal year 2010's authorization of $69.955 million. Of this amount, $10 million is dedicated to needed transportation capital expenditures throughout the State. The overall recommendation will allow for additional funding of capital projects without significant deterioration of key financial ratios used by rating agencies. It also maintains the State's credit posture as a triple-A rated state.**

In March, the Treasurer's Office sold approximately $50 million in General Obligation bonds. The opportunity to purchase the bonds was offered first to Vermont residents and businesses and could be purchased in $1,000 increments. Demand was extremely high with the bonds selling out in less than three hours. To raise awareness of the bond sale, the Treasurer's Office ran notices like the one above on the internet, in addition to other advertising.

Debt Management
(802) 828-5197

Stephen Wisloski
Investment & Debt Management Director

Wisloski Joins Treasurer's Office Team

Stephen Wisloski assumed the position of Director of Investment and Debt Management in July 2009. Wisloski has more than 12 years of broad-based municipal finance experience. He is a graduate of the Massachusetts Institute of Technology and of Essex High School. "I am thrilled at the opportunity to work with the Treasurer's Office, and to leverage my private sector experience to the benefit of the citizens of Vermont," said Wisloski.

Stephen Wisloski

Wisloski worked for 12 years for two subsidiaries of the PFM Group, one of the nation's leading providers of independent financial and investment advisory services. As a senior managing consultant for Public Financial Management, Wisloski led business development efforts for environmental utilities throughout the western United States. In a similar role for PFM Asset Management, he assisted clients in investment policy development, proposal evaluation, and ongoing risk management and reporting. He worked from the company's San Francisco, California offices.

Prior to working at PFM, Wisloski served for three years in the United States Air Force as an acquisition program manager and received an Air Force Commendation Medal for distinguished service. He joined the Air Force upon graduating from MIT with a bachelor of science degree in political science. Wisloski attended MIT through a four-year academic scholarship from the U.S. Air Force Reserve Officers' Training Corp.

Wisloski replaced David Minot, who resigned to pursue another opportunity in the private sector.

- The downgrade and subsequent exit from the market of all but one municipal bond insurer, and the dramatic reduction of the use of bond insurance policies from over half of all bonds issued in 2007 to barely 10 percent in 2009.

- Severe impacts to variable rate securities, including the dissolution of the auction rate securities market, and substantially increased costs of liquidity and credit support for variable rate demand bonds.

- The disappearance of many leveraged institutional buyers of municipal bonds, and the re-appearance of retail (that is, "Mom and Pop") investors.

Against this dire backdrop, the State of Vermont has benefitted from disciplined debt issuance and debt management policies. These policies include moderate levels of bond issuance, careful consideration of debt affordability, strict adherence to credit rating agency guidelines, and strong fiscal budget policies to ensure that the State has funds readily available for bond principal and interest payments. In addition, the State has struck a balance between competitive bond sales, which are the preferred alternative of Vermont's triple-A rated peer states, and negotiated sales, which ensure retail distribution of the State's bonds to Vermont-based investors.

These efforts are the result of years of attention to rating agency and investor interests and concerns and have resulted in the high debt rating that the State currently enjoys, and customer diversification from distribution of Vermont bonds to both institutional and retail investors. As a result, Vermont can expect, even in a severe credit environment, to be able to cost-effectively issue its G.O. Bonds and meet its infrastructure and other capital expenditure needs, unlike many less creditworthy issuers. The next G.O. Bond issues are scheduled for January and February of 2010. Continuing with Vermont's efforts to diversify its investor base, the larger January issue will be sold on a competitive basis, and the smaller February "Vermont Citizens Bond" issue will be sold on a negotiated basis to Vermont-based retail investors.

Overview

The Treasurer's Office, in conjunction with the Administration and State Legislature, has historically set a course of maintaining modest levels of new authorizations of long-term debt and net tax-supported debt outstanding. As a result, bond issuance is currently at substantially lower levels than in the early and mid-1990s. Reduction in debt, plus continued improvement in the State's economic indices and financial condition over recent years, have improved the State's debt ratios to those among the highest-rated states. The State's practice of issuing debt with level annual principal installments has also resulted in a favorable amortization rate. At a rate of 76.1 percent retirement within ten years, the State's bond payoff ratio continues to be favorably received by the rating agencies.

A major contributing factor to Vermont's respected debt management is the work of the Capital Debt Affordability Advisory Committee (CDAAC). The CDAAC completes an annual review of the size and affordability of the State tax-supported general obligation debt and submits to the Governor and to the General Assembly an estimate of the maximum amount of new long-term general obligation debt that prudently may be authorized for the next fiscal year. The estimate of the committee is advisory, but historically has been adopted by the State as a bonding limit. The CDAAC is made up of three ex officio members, two appointees of the Governor, one appointee of the State Treasurer, and an appointee of the Vermont Municipal Bond Bank. The State Treasurer serves as chair of the committee.

In September of 2009 the CDAAC set the fiscal year 2011 recommended debt authorization level at $71.825 million, which is the highest level that allows for adherence to CDAAC guidelines, notwithstanding creation of higher levels of debt outstanding. The committee continues to believe that debt issuance moderation is appropriate in uncertain economic times. Of this amount, $10 million is allocated to transportation capital expenditures.

Reduction in debt, plus continued improvement in the State's economic indices and financial condition over recent years, has improved the State's debt ratios to those among the highest-rated states.

The State's disciplined approach to debt management is paying off in today's tax-exempt marketplace. By practicing debt issuance moderation and compliance with well defined guidance standards that have the clear goal of Vermont being a triple-A rated state, Vermont has the ability under current challenging credit market conditions to issue debt at attractive interest rates to meet infrastructure and other capital spending needs. Providing for a significant level of transportation expenditures within the capital budget is, with regard to recent history, a change for the State, and welcome in the context of needed transportation projects spending.

UPDATES

Bond Issues

The State Treasurer's Office issued $50.5 million aggregate principal amount of new money G.O. Bonds in fiscal year 2009, with a true interest cost of 3.82 percent and an average life of 10.5 years. Especially given market conditions at the time, the State's strong bond ratings discussed above were a key factor in enabling the State to access markets that were essentially frozen to all but the highest-quality issuers. It also allowed the State to obtain very favorable interest rates.

The Treasurer's Office has scheduled two G.O. Bond sales in fiscal year 2010, a $52 million competitive sale (2010 Series A) in January, and a $20 million negotiated Vermont Citizens Bond sale in February 2010 (2010 Series B). The use of both competitive and negotiated sales allows the State to achieve the dual goals of using the "best practices" of triple-A states (competitive sales), while maintaining a Vermont-based retail investor base, which can only be assured by using a negotiated sale. In addition, the State is monitoring opportunities to refinance existing debt to achieve cost savings.

Bond Rating

Vermont was assigned an Aaa rating by Moody's in February of 2007. Vermont shares its Moody's triple-A rating with only nine other states. As of December 2009, only thirteen states have a triple-A rating from at least one rating agency. Combined with AA+ bond ratings from both S&P and Fitch, Vermont enjoys the highest general obligation bond ratings of any New England state (see bond rating chart below). With all three ratings carrying a "Stable" outlook, Vermont continues to work toward achieving a triple-A rating from S&P and Fitch.

The triple-A rating by Moody's and the excellent ratings by Fitch and S&P are reflective of sound fiscal practices that include: (1) budgetary discipline; (2) an economy with significant breadth; (3) strong debt management practices; and (4) effective State governance reflecting sound statutes and legislative history.

Like most states, Vermont is experiencing budgetary pressures brought about by a credit crisis and a national and state economy in recession. Traditionally, Vermont has managed economic downturns very well in comparison to other states, with a resilient economy and strong fiscal and debt management practices.

The current downturn, while not over, has been no exception to date. Vermont's unemployment rates, while high, are relatively favorable compared to New England and other states. Just as important, the State's response with regard to sound fiscal policy has been prompt and decisive. With periodic revenue downgrades and expense cuts to match, the State is maintaining a balanced budget with reserve funds available only as a last resort. This discipline is recognized by rating agencies and investors alike, and contributes to both favorable bond ratings and favorable investor perceptions of the State.

Because a higher rating enhances the State's reputation in the municipal marketplace, it makes Vermont's bonds very marketable to a broad range of individual and institutional investors. As noted previously, this generally results in a lower interest rate or cost of capital for borrowing. It also is likely to reduce borrowing costs for municipalities that issue debt through the Vermont Municipal Bond Bank or other borrowers issuing State moral obligation debt through other State agencies, as the State's rating supports these bond issues. A high credit rating also is attractive to business development because it is a sign of economic and fiscal stability.

New England General Obligation Bond Ratings

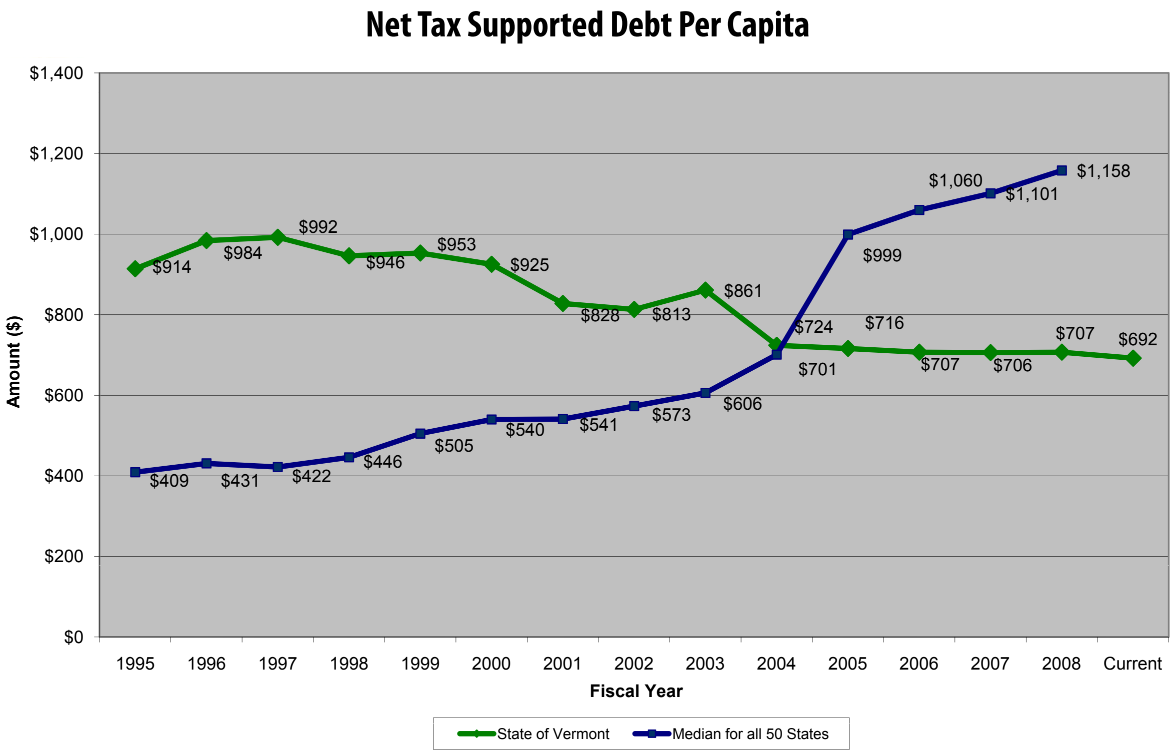
STATE	FITCH	MOODY'S	S&P
Vermont	**AA+**	**Aaa**	**AA+**
Connecticut	AA	Aa3	AA
Maine	AA	Aa3	AA
Massachusetts	AA	Aa2	AA
New Hampshire	AA	Aa2	AA
Rhode Island	AA-	Aa3	AA

Debt Ratios

The fiscal discipline of recent years has paid off as Vermont's debt ratios rank favorably among triple-A rated states. In fiscal year 2007, Moody's recognized this and upgraded Vermont from Aa1 to Aaa. The key to maintaining and obtaining other triple-A ratings will be to demonstrate continued diligence in the areas just discussed while making improvements on other major sustainability issues. Thos issues are: Medicaid funding; State employees' and teachers' pension funding; the funding of other post-employment benefits (OPEBs); and preservation and development of the State's infrastructure. Summarized below are some of the key debt indicators for Vermont.

Debt Per Capita

One of the key debt factors monitored by the CDAAC and the rating agencies is the State's net tax-supported debt per capita. The guideline adopted by the CDAAC establishes a target debt per capita at Moody's median and means for triple-A rated states. In 2009, the State's debt per capita was $692 versus the Moody's five-year triple-A median and mean of $778 and $896, respectively (see chart facing page). The State's ranking versus all 50 states improved steadily from 28th in 2007, to 32nd in 2008, to 34th in 2009. The higher the ranking figure, the lower a state's debt per capita is relative to all other states. This 2009 ranking is considerably above average; only 16 states have a higher (more favorable) ranking figure. Currently, the State's debt per capita is $692. The State's net tax-supported debt per capita is forecast to grow to $1,098 by 2020. That forcast assumes a steady level of debt authorization and the issuance of $71.825 million in future years starting in fiscal year 2011, and employs the population forecast developed by Economic Policy Resources. This increase, over a significant period of time, is



expected to remain consistent with the State's debt per capita guideline (triple-A states five-year median and mean) each year through 2020.

Debt as a Percentage of Personal Income

An even more important credit factor for assessing a state's relative ability to pay its general obligation debt is the ratio of net tax-supported debt as a percent of personal income. The guideline adopted for this ratio is again to target Moody's five-year median and mean for triple-A rated states. The State has steadily improved in this area. The State's ratio of debt to personal income for fiscal year 2009 dropped to 1.8 percent versus Moody's triple-A median and mean ratios of 2.5 percent and 2.7 percent, respectively (see chart next page). The State's ranking in its debt as a percentage of personal income improved steadily from the 30th highest among all states in 2007, to 33rd highest in 2008, to 35th highest in 2009.

Debt as a Percentage of Revenue

The guideline used for this ratio states that projected annual State debt service on bonds should not be in excess of 6 percent of projected revenues in the combined General and Transportation Funds. The debt service as a percentage of revenues ratio was 5.5 percent for fiscal year 2009. This percentage is expected to rise to 5.7 percent in fiscal years 2010 and 2011, and then decline through fiscal year 2020. This is based on the assumption of the issuance of $71.825 million of debt from fiscal year 2011 through fiscal year 2020.

Additional Factors Affecting Bond Ratings

There are many other factors considered in a state's bond rating besides ratio analyses. These include:

- **Budget Stabilization Reserves:** The State has budget stabilization reserve levels required by statute for each of the State's General Fund, Transportation Fund, and Education Fund. Required reserves for the General Fund and

Moody's Investors Service -- Debt Per Capita -- State of Vermont

Triple-A Rated States	July, 2009 Ratings			2005	2006	2007	2008	2009
	Moody's	S&P	Fitch					
Delaware	Aaa/Stable	AAA/Stable	AAA/Stable	$1,865	$1,845	$1,998	$2,002	$2,128
Florida[1]	Aa1/Negative	AAA/Negative	AA+/Negative	1,008	976	1,020	1,005	1,115
Georgia	Aaa/Stable	AAA/Stable	AAA/Stable	803	784	916	954	984
Indiana[2]	Aa1/Stable	AAA/Stable	AA/Stable	415	474	657	478	482
Iowa[3]	Aa1/Stable	AAA/Stable	AA+/Stable	130	110	104	98	79
Maryland	Aaa/Stable	AAA/Stable	AAA/Stable	1,064	1,169	1,171	1,297	1,507
Minnesota	Aa1/Stable	AAA/Stable	AAA/Negative	679	746	827	879	866
Missouri	Aaa/Stable	AAA/Stable	AAA/Stable	449	496	613	675	670
No. Carolina	Aa1/Stable	AAA/Stable	AAA/Stable	682	804	728	898	832
So. Carolina	Aa1/Stable	AA+/Stable	AAA/Stable	558	661	630	966	899
Utah	Aaa/Stable	AAA/Stable	AAA/Stable	792	707	621	542	447
Virginia	Aaa/Stable	AAA/Stable	AAA/Stable	589	601	692	764	782
MEAN[4]				**831**	**879**	**922**	**951**	**899**
MEDIAN[5]				**682**	**765**	**778**	**898**	**849**
VERMONT[6]	Aaa/Stable	AA+/Stable	AA+/Stable	716	707	706	707	692

Triple-A Rated States--5-Year Average Mean and 5-Year Median Excluding Vermont

MEAN: $896 VERMONT: $706 MEDIAN: $778 VERMONT: $706

See footnotes bottom of this page.

Moody's Investors Service -- Debt as % of Personal Income -- Vermont

Triple-A Rated States	2005	2006	2007	2008	2009
Delaware	5.5%	5.3%	5.5%	5.2%	5.4%
Florida[1]	3.4	3.2	3.1	2.8	2.9
Georgia	2.8	2.7	3.0	3.0	3.0
Indiana[2]	1.4	1.4	2.1	1.5	1.5
Iowa[3]	0.5	0.4	0.3	0.3	0.2
Maryland	2.9	3.0	2.8	3.0	3.3
Minnesota	2.0	2.1	2.2	2.3	2.1
Missouri	1.5	1.6	1.9	2.1	2.0
North Carolina	2.5	2.8	2.4	2.8	2.5
South Carolina	2.2	2.5	2.3	3.3	2.9
Utah	3.2	2.7	2.3	1.9	1.5
Virginia	1.8	1.7	1.8	1.9	1.9
MEAN[4]	**2.7**	**2.8**	**2.7**	**2.8**	**2.4**
MEDIAN[5]	**2.5**	**2.7**	**2.3**	**2.8**	**2.3**
VERMONT[6]	2.3	2.2	2.1	2.0	1.8

Triple-A Rated States--5-Year Average Mean and 5-Year Median Excluding Vermont

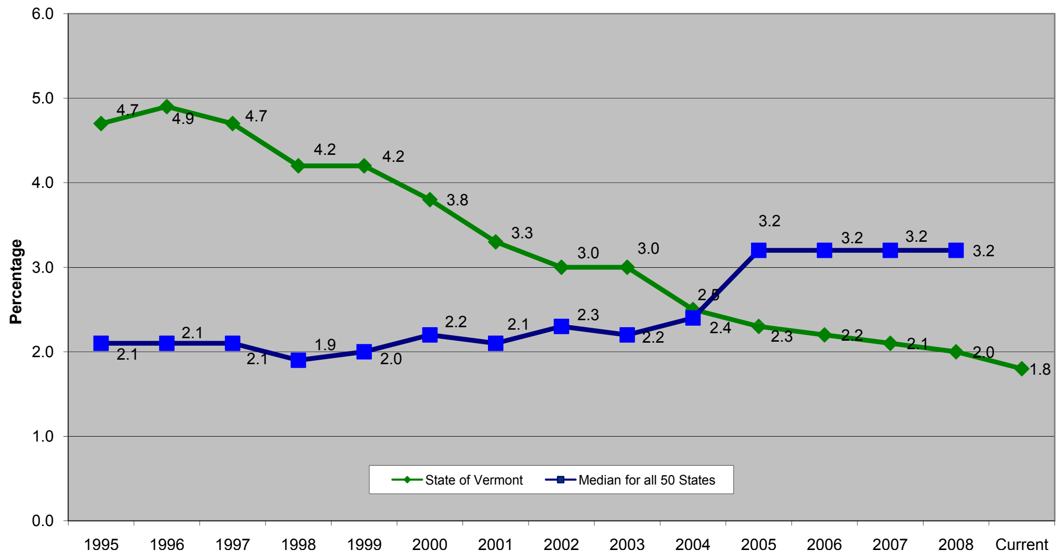
MEAN: 2.7% VERMONT: 2.1% MEDIAN: 2.5% VERMONT: 2.1%

See footnotes bottom of this page.

FOOTNOTES FOR ABOVE CHARTS

1 Florida raised to triple-A in 2005 and first reflected in 2006 numbers.
2 Indiana carries Municipal Issuer Ratings from both Moody's and S&P, assigned in 2008 and first reflected in 2008 numbers – this is a GO bond equivalent rating as Indiana does not have GO debt outstanding; the Fitch rating is for lease revenue bonds.
3 Iowa carries Municipal Issuer Ratings from Fitch, Moody's and S&P, assigned in 2009 and first reflected in 2009 numbers – this is a GO bond equivalent rating as Iowa does not have GO debt outstanding.
4 These calculations exclude all Vermont numbers.
5 These calculations exclude all Vermont numbers.
6 Vermont raised to triple-A in 2007.

Net Tax Supported Debt as a Percentage of Personal Income



Transportation Fund are 5 percent, and for the Education Fund are 3.5 percent to 5 percent of the previous year's appropriations. Currently, all three funds are at their statutory requirements and as stated above, have not yet been tapped in response to the current economic downturn. In addition, the State has human services caseload reserves which at June 30, 2009, were over $16 million. The combined effect of full budget stabilization reserves plus the caseload reserves is positive for the State's ratings.

- **Pension Funds Funding Percent:** Of the three State-level pension funds, two receive State contributions—the Vermont State Employees' Retirement System (VSERS) and the Vermont State Teachers' Retirement System (VSTRS). Inasmuch as State contributions derive from taxes, the rating agencies are very concerned with the percentage of future pension liabilities that are funded in these plans. As of June 30, 2009, the VSERS funding level is at 78.9 percent and the VSTRS funding level is 65.4 percent–down from 94.1 percent and 80.9 percent–indicating that both are under-funded. While budgets are squeezed as a result of the recent economic downturn, continued discipline in funding the actuarial required contribution (ARC) is an important factor for the rating agencies. The Commission on the Design and Funding of Retirement and Retiree Health Care Benefit Plans for State Employees and Teachers has made recommendations on benefit changes that address the long-term sustainability of the system. While the commission believes that the recommendations represent a sound direction, they also recognize that there are a range of options that will be reviewed during this legislative session. A solid plan to achieve sustainability and to continue the discipline of full funding of the ARC is needed. Other post-employment benefits (OPEBs), beyond pension benefits, to retired system participants also are of interest to the rating agencies. While Vermont's OPEBs have minimal funding for VSERS and none at present for VSTRS, the State has undertaken studies over the past three years to analyze the size of these obligations and assess alternative funding strategies. This effort is recognized by the rating agencies, although continued progress is necessary.
- **Other Factors:** The rating agencies also consider the breadth of the economy; the level and condition of the State's transportation, utilities and other infrastructure; personal income levels; fiscal responsibility; employment levels; workforce size and training; population demographics and trends; internal controls and auditing standards; need for short-term borrowings; and other factors.

Approach Toward Establishing Debt Ratio Goals -- State of Vermont

Comparative Mean Debt Ratios[1]

Per Capita	2005	2006	2007	2008	2009
All States	$ 999	$1,060	$1,101	$1,158	$1,195
Triple-A[2]	831	879	922	998	899
VERMONT	**716**	**707**	**706**	**707**	**692**
% of Pers. Inc.	**2005**	**2006**	**2007**	**2008**	
All States	3.2%	3.2%	3.2%	3.2%	3.1%
Triple-A[3]	2.7	2.8	2.7	2.8	2.4
VERMONT	**2.3**	**2.2**	**2.1**	**2.0**	**1.8**

1 Based on data provided by Moody's Investors Service. Florida raised to triple-A in 2005 and first reflected in 2006 numbers; Indiana carries Municipal Issuer Ratings from both Moody's and S&P, assigned in 2008 and first reflected in 2008 numbers – this is a GO bond equivalent rating as Indiana does not have GO debt outstanding; the Fitch rating is for lease revenue bonds; Iowa carries Municipal Issuer Ratings from Fitch, Moody's and S&P, assigned in 2009 and first reflected in 2009 numbers – this is a GO bond equivalent rating as Iowa does not have GO debt outstanding; these calculations exclude all Vermont numbers.
2 See chart on "Debt Per Capita" for complete listing of triple-A states and respective ratings. Thirteen states currently rated triple-A by one or more of the nationally recognized rating agencies: Delaware, Florida (2005), Indiana (2008), Iowa (2008), Georgia, Maryland, Minnesota, Missouri, North Carolina, South Carolina, Utah, Virginia and Vermont (2007).
3 Same as Footnote #2.

Short-Term Borrowing

The seasonal nature of the revenue and expenditure cycles occasionally requires the use of short-term borrowing. Typically, education payments to local towns and school districts occur in the first half of the fiscal year, while tax revenues are collected later in the year, primarily April. By April the revenue flow is generally positive. In the early 1990s, Vermont was issuing approximately $150 million of short-term debt obligations annually, not including $65 million in deficit notes. The State did not require the issuance of short-term debt in fiscal years 1999-2002. With the economic decline in 2002, the State issued $75 million in revenue anticipation notes (RANs) for part of 2003 and $48 million in September to early March 2004. While the State has had a line of credit available to it during the last five years, it has not had to access it, a continuing sign of fiscal health. Current economic conditions and declining State revenues require monitoring in the context of short-term borrowing needs. The State has been diligent in managing expenditures according to revised revenue projections, and, despite experiencing some stresses, did not need to borrow funds in either September or December of 2009. At this point it is unclear what borrowing levels, if any, will be needed for the balance of fiscal year 2010. If the State is required to borrow funds, such needs are planned to be met using the letter of credit, which can be repaid immediately. Using the letter of credit is preferable to longer-term financing alternatives such as RANs, which would generate higher interest costs for the State. The State began fiscal year 2009 with approximately $279.8 million in unrestricted cash and investments on hand and ended the year with $235.6 million in unrestricted cash and investments. While these cash balances do not bear a direct one-to-one relationship to fund balance, they indicate a stable and solid position as of fiscal year 2009.

Investments

Overview

The State Treasurer's Office is responsible for investment of the State's short-term and operating funds and certain trust funds, and is the administrative arm for the retirement boards and the Vermont Pension Investment Committee. Short-term operating funds are invested by the Treasury Operations Division, which also is responsible for banking and cash management and projections. These funds are invested based on the Treasurer's authority in State statute. The State Treasurer has issued further guidelines for these investments, consistent with statute. The guidelines are available on the Treasurer's Office web site at http://www.vermont-treasurer.gov/cash/index.html. The guiding principles for these investments are safety followed by liquidity and yield.

Certain trusts, including the Higher Education Trust Fund, Tobacco Trust Funds, a State OPEB Trust Fund and other trusts are pooled and invested in a Trust Investment Account (TIA). The Trustee for these funds is the State Treasurer. The Director of Investment and Debt Management provides administrative support, including due diligence and portfolio review. Treasury Operations reconciles the investment management and custodian reports and maintains the financial statements. Investment of funds is delegated to four investment managers, three of

Investments
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Stephen Wisloski
Investment & Debt Management Director

John Booth
Treasury Operations Director

Dan Currier
Cash & Investments Manager

Donna Holden
Contracts & VPIC Coordinator

ACCOMPLISHMENTS IN 2009

- **While the Federal Reserve response to the economic crisis had the effect of lowering short-term money market rates, the State Treasurer's Office short-term investments exceeded the established benchmarks of the average three-month Treasury bill yield, earning 1.56 percent as compared to the benchmark of 0.54 percent during the fiscal year.**

- **As part of the Vermont Pension Investment Committee's continued diversification efforts, a new asset allocation was adopted and no fewer than seven new investment managers were added in the categories of core plus fixed income, risk parity, mid-cap domestic equities, high-yield debt, emerging market debt, U.S. Treasury inflation-protected securities (or "TIPS"), and commodities.**

- **Two of the new investment managers, Champlain Investment Partners, LLC and KDP Asset Management Inc., were selected from nine finalists in the VPIC's highly competitive "Vermont Manager Program." Under this new initiative, a Request for Proposals was distributed to 215 Vermont-based banks and investment managers. Using a "buy local" approach, the program aims to support the growth and success of the investment management business in Vermont.**

- **To further its efforts to protect against down-side losses in the pension funds, the VPIC also distributed a Risk Management Request for Information and reviewed responses from 12 firms from the United States, Canada and Europe. VPIC plans to meet with several of these firms in early 2010 and consider whether to engage a full-time risk manager.**

Program Taps Local Investment Expertise

Using a "buy local" approach, a new State program aims to support the growth and success of the investment management business in Vermont. In 2009, VPIC contracted with two Vermont-based firms to manage a portion of the roughly $2.9 billion in assets for the State pension systems. The Vermont Manager Program was adopted as a targeted effort to utilize locally provided investment management services from firms capable of offering world-class institutional management at competitive costs. Following a request for proposals, and subsequent presentations and interviews, Champlain Investment Partners of Burlington and KDP Asset Management of Montpelier were selected to each manage approximately $21 million in assets.

"Our belief is that the Vermont Manager Program will help build Vermont's infrastructure for investment management firms, while providing excellent investment results for members and beneficiaries of the State's pension system," said VPIC Chair Stephen Rauh.

A notice of the request for proposals was sent to more than 200 registered investment advisors throughout Vermont. The RFP sought proposals to manage assets within VPIC's current equity and fixed income asset allocation. Champlain Investment Partners was founded in 2004 and is a registered investment advisor focused on small and mid-cap equity investment strategies. KDP Investment Advisors has done business in Vermont since 1975. It is an independent company wholly owned by its management and employees and provides a variety of corporate high yield bond research and portfolio management services.

Contracts with the two firms are for five years and may be automatically renewed by VPIC.

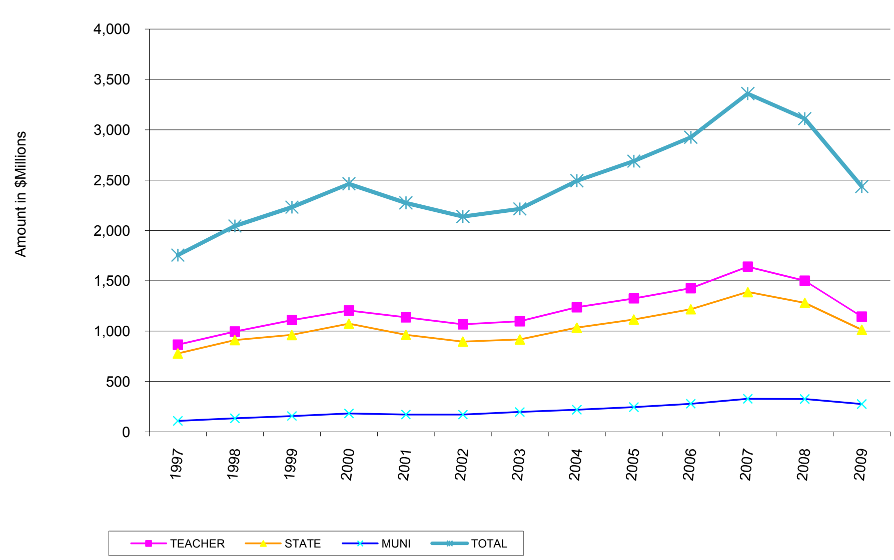
whom are Vermont-based firms. The fourth manager invests in mortgage securities, creating capital for Vermont. Peoples United Bank (formerly Chittenden Bank) provides custody services.

The retirement boards act as trustees for various benefit-related trusts including two defined contribution plans (State and municipal), a single deposit investment account or SDIA (State and teachers), a deferred compensation fund (open to teachers, municipal, and State members, with the State Retirement Board acting as trustee), and a Municipal Employees' Health Benefit Fund. All employ outside managers. The Director of Investment and Debt Management and other staff provide due diligence and portfolio review, as well as contract compliance and reconciliation functions.

The Vermont Pension Investment Committee (VPIC) acts as the trustee for the defined benefit plan investments. The board of trustees for each system maintains its fiduciary role in the area of benefits administration, actuarial recommendations, and asset allocation. In 2007, the legislature passed legislation enabling municipalities not participating in the municipal defined benefit plan to pool their assets in VPIC for investment purposes. During fiscal year 2008, the City of Burlington transferred assets to the VPIC, effective the end of October 2007. VPIC is therefore classified as an external investment pool, investing the funds for Burlington and the three defined benefit plans (State, teachers, municipal).

With respect to pensions, the VPIC employs an outside investment consultant, New England Pension Consultants (NEPC), to assist them in their fiduciary responsibility, including development of investment policies and objectives; risk management assessment and asset allocation plans; investment manager and custodian searches; monitoring of management performance; industry issues; SEC compliance; and on-going due diligence on investment managers, performance measurement, and education on various issues (asset classes, alternative investments, risk assessment). The Director of Investment and Debt Management and other staff provide administrative support including rebalancing the portfolio, portfolio review and due diligence, and instructions to managers to receive/remit cash to fund benefit programs, based on projections provided by Treasury Operations.

Growth of Pension Assets -- Fiscal Year 1997-2009



UPDATES

Higher Education Trust Fund

The 1999 State Legislature established the Vermont Higher Education Endowment Trust Fund and appropriated $6 million for the creation and management of the fund by the State Treasurer. An additional $1 million was added to the fund in fiscal year 2001--$635,881 at the end of fiscal year 2002; $2,363,355 in fiscal year 2006; $5,823,450 in fiscal year 2007; and $57,209 in fiscal year 2008. On June 30, 2009, the fund had a market value of $17,050,798.96. In September of 2009, the State Treasurer authorized the distribution of 5 percent of the average market value of the assets over the prior 12 quarters equally among the University of Vermont, the Vermont State Colleges, and the Vermont Student Assistance Corporation. Each entity received $290,892.03 to be applied as non-loan financial aid to Vermont students attending Vermont post-secondary institutions.

The Higher Education Endowment Trust Fund Act further provides that contributions shall include "… in any fiscal year in which a general fund surplus exists and the general fund stabilization reserve is funded to its required statutory level, funds raised by the estate tax under chapter 190 of Title 32 which are more than 125 percent of the amount projected by the emergency board in the July annual forecast made pursuant to section 305a of Title 32." In fiscal year 2008, a substantial contribution from this provision was made of $5,223,449.94 derived from fiscal year 2006. This contribution became part of the Higher Education Trust Fund early in fiscal year 2007. In addition, pursuant to legislation introduced by the Treasurer, all unclaimed property worth less than $100 that has been under State custody for ten years or longer is to be turned over to the Higher Education Trust Fund. In the first year of this provision deriving from fiscal year 2006, $600,000 was added to the fund in fiscal year 2007. While the contributions from these sources were small in fiscal year 2008, and there were no contributions in fiscal year 2009, over time these statutory provisions are expected to make significant contributions to this fund.

In addition to the above disbursements from the fund, the Vermont Commission on Higher Education Funding authorized the Treasurer to make available the additional 2 percent distribution of $298,227.18 to be divided equally between the University of Vermont and the Vermont State Colleges for application to their respective permanent endowments. In fiscal year 2010, the additional endowment allocation will be $174,535.22 for each institution, provided that it is matched on a two-to-one basis by external donations for endowment purposes by the end of the fiscal year and subject to statutory limitations on distributions exceeding contributions. A copy of the State Treasurer's Annual Report to the Commission is attached at the back of this report in the appendix section.

Trust Investment Account

The 2000 State Legislature authorized the establishment of a trust investment account administered by the State Treasurer for purposes of investing restricted funds with non-expendable principal balances. As of June 30, 2009, the fund had a principal balance of approximately $59.2 million, of which $33.9 million was allocated to the Tobacco Trust Fund, $17 million to the Higher Education Endowment Trust Fund, and the remainder to various smaller trust funds. The current target allocation of the Trust Investment Account is 70 percent fixed income securities and 30 percent equities. For fiscal year 2009, the fund had a dollar weighted total return of 2.40 percent versus the target return of negative 1.19 percent, which is based on actual asset allocation, and the performance of the S&P 500 Stock Index (negative 26.21 percent) and the Barclays (formerly Lehman) Ag-

VPIC Membership

The Vermont Pension Investment Committee is responsible for investing almost $2.5 billion in assets for the three state-level retirement systems as of June 30, 2009. Act 100, which became effective July 1, 2008, redefined the membership of VPIC to six voting members and four alternates (from seventeen members previously). The active and retired employee members of the Vermont State Employees' Retirement System and Vermont State Teachers' Retirement System boards of trustees each appoint one member and one alternate. The employee and municipal official members of the board of the Vermont Municipal Employees' Retirement System appoint one member and one alternate. In addition, two members and one alternate are appointed to the VPIC by the Governor. The sixth member is the State Treasurer or designee. In considering appointments, the legislation directs that the experience and knowledge of potential appointees be considered in light of the purposes of the committee. The members serve staggered four-year terms with no term limits.

As of June 30, 2009, individuals appointed to the committee are: Warren Whitney, VSERS voting member; Robert Hooper, VSERS alternate; Stephen Rauh, VMERS voting member; Steven Jeffrey, VMERS alternate; Joseph Mackey, VSTRS voting member; Jon Harris, VSTRS alternate; Richard Johannesen, Governor's appointee; Michael K. Smith, Governor's appointee; Vaughn Altemus, Governor's alternate; and Jeb Spaulding, State Treasurer.

gregate Bond Index (6.06 percent).

In fiscal year 2008, the Treasurer's Office invested $2.5 million of Trust Investment Account (TIA) assets in a mutual fund that invests in public housing and other fixed income securities throughout the United States. The balance continues to be invested and earning interest. The fund manager, Access Capital, has an equal investment in high-grade Vermont securities that address principally underserved segments of the housing market, such as affordable housing. The aim of the investment was to increase the pool of available capital funds for affordable housing in Vermont.

Access Capital invests in mortgages to homebuyers making less than 80 percent of an area's median income. With the median income reported for all Vermont households now at approximately $50,000, the investments expand home mortgage loan opportunities for households making, on average, less than $40,000 a year. The recent loan default problems in the subprime mortgage lending market combined with all other credit market conditions has tightened the availability of funds for home loans to low-income households. However, unlike in the subprime lending market, potential homebuyers must go through a tougher loan approval process before being granted a federally-qualified mortgage. Since the loans structured and purchased by Access Capital are federally-qualified mortgages, the investments are more secure. The fund invests primarily in AAA/credit quality community economic development investments, usually specially created mortgage-backed securities.

FUND PERFORMANCE & OPERATIONS

Pension Fund Investments

VPIC oversees all investment assets held by the Vermont State Employees' Retirement System, the State Teachers' Retirement System of Vermont, and the Vermont Municipal Employees' Retirement System. The three systems had combined assets of approximately $2.44 billion on June 30, 2009. In addition, the Burlington Employees' Retirement System, which became a participating investor with the VPIC at the end of October 2007, had assets of approximately $89.9 million as of the same date. In fiscal year 2009, one-year investment returns were negative 18.7 percent for VSERS, negative 19.8 percent for VSTRS, and negative 18.2 percent for VMERS versus the median public fund return of negative 16.6 percent (see chart below) For the ten years ending June 30, 2009, the median public retirement plan in the consultants' cooperative had an average annualized total return of 3.1 percent, compared with 2.9 percent for VSTRS, 2.5 percent for VSERS, and 2.8 percent for VMERS.

Long-term Investment Performance of Vermont's Retirement Systems (As of June 30, 2009)

Gross of Fees

Retirement System:	Last 1 Year	Last 3 Years	Last 5 Years	Last 7 Years	Last 10 Years
Teachers Composite	-19.8%	-4.2%	1.3%	3.8%	2.9%
State Composite	-18.7%	-3.7%	1.4%	3.8%	2.5%
Municipal Composite	-18.2%	-3.6%	1.5%	3.4%	2.8%
Median Public Fund	-16.6%	-2.3%	2.4%	4.4%	3.1%

Source: New England Pension Consultants

Long-term Investment Performance of Vermont's Retirement Systems (As of September 30, 2009)

Gross of Fees

Retirement System:	Since January 1	Last 3 Years	Last 5 Years	Last 7 Years	Last 10 Years
Teachers Composite	22.7%	-1.2%	3.9%	7.3%	4.5%
State Composite	23.5%	-0.8%	4.0%	7.3%	4.0%
Municipal Composite	24.2%	-0.6%	4.3%	6.9%	4.5%
Median Public Fund	15.1%	-0.3%	4.2%	7.0%	4.3%

Source: New England Pension Consultants

Notwithstanding the negative returns for the prior 12 months, the total returns for the Vermont Retirement Systems have rebounded substantially from the beginning of 2009 (see chart above). As of September 30, 2009, the year-to-date investment returns were 23.5 percent for VSERS, 22.7 percent for VSTRS and 24.2 percent for VMERS. These returns ranked in the 6th, 8th, and 2nd percentiles, respectively, meaning they exceeded the returns of more than 90 percent of comparable public-sector funds.

This performance was primarily due to VPIC maintaining its discipline with respect to asset allocation. For example, during the March 2009 bottom in equity prices due to depressed market values, VPIC's equity managers were, for the most part, well below their target asset allocation percentages relative to the portfolio. Fixed income managers were above their target allocations. As part of its regularly-scheduled rebalancing process, VPIC shifted funds from fixed income managers to equity managers, to align the respective managers back to their target asset allocations. From March through September, equity prices surged, and during the September rebalancing, VPIC shifted funds from equity manag-

Asset Allocation of Pension Funds as of June 30, 2009

Investment Category	Teacher	State	Municipal
Equity			
Domestic Large Cap	30%	26%	26%
Domestic Small/Mid Cap	13%	13%	11%
International Established	13%	13%	13%
Emerging Market	4%	4%	4%
Total Equity	59%	56%	53%
Fixed Income			
Core Plus/Portable Alpha	10%	13%	15%
High Yield Bonds	5%	5%	5%
Global Bonds	4%	4%	2%
Total Fixed Income	19%	22%	23%
Alternatives			
Real Estate	6%	5%	5%
Total Alternatives	6%	5%	5%
Multi-Strategy			
All-Asset/Global Asset Allocation	16%	17%	18%
Total Multi-Strategy	16%	17%	18%
Grand Total	100%	100%	100%

ers back to fixed income, effectively locking in the market gains. This was not a "market call" or an emotionally-driven decision, but rather part of the VPIC's disciplined, consistent approach to risk management through diversification and asset allocation.

At the same time, these very favorable returns, coming on the heels of steep negative returns, suggested considerable volatility in the portfolio. As a result, VPIC also continued efforts to diversify the portfolio and maintain competitive investment returns while lowering risk. To do this, VPIC engaged managers in core plus fixed income, risk parity, emerging market debt, U.S. Treasury inflation-protected securities (TIPS), and commodities. VPIC also adopted a new asset allocation that lowered the target equity allocation of the portfolio from more than 57 percent equities to 42.5 percent, and increased the fixed income allocation from under 21 percent of the portfolio to 36 percent. Finally, to streamline administration and ensure greater consistency of returns across the three retirement systems, VPIC is migrating all three Vermont Retirement Systems to the same asset allocation.

These very favorable returns, coming on the heels of steep negative returns, suggest considerable volatility in the portfolio. VPIC will continue efforts to diversify the portfolio and maintain competitive investment returns while lowering risk.

Through a competitive process, in fiscal year 2008 the VPIC selected a consultant and advisor to assist with its previously adopted policy relating to investing in companies involved in genocidal or terrorist states. VPIC had previously requested divestiture of one issuer held on two VPIC accounts. The request was accommodated. With assistance from this advisor, the VPIC has the tools required to identify issuers that may be in conflict with its policy and proceed with engagement or divestiture as appropriate. The VPIC continues to discuss this policy and ways of enhancing its efficacy in engaging or divesting companies found to be in conflict with it.

Proxy voting guidelines adopted in March 2004 continued to be in effect in fiscal year 2008. In calendar 2007, VPIC engaged a proxy voting firm to vote its equity securities in accordance with these guidelines, in place of investment manager voting. As a result of the passage of time, this contract expired in calendar 2008 and a competitive process was undertaken for selection of the advisor. The corporate governance guidelines include voting policies relating to boards of directors, auditors, shareholder rights, and executive and director compensation. The policy's corporate responsibility and accountability guidelines include voting policies on environmental issues such as global warming and environmental reporting, as well as workplace issues such as equal employment opportunities, human rights, and labor codes. This policy can be viewed on the State Treasurer's web site.

Trust Litigation Settlement Fund and the Tobacco Trust Fund

In November 1998, Vermont was one of 46 states to enter into a settlement agreement with four major tobacco companies. The State's estimated share of settlement payments at that time was expected to total $806 million over the first 25 years of payment, with an additional $156 million of strategic contribution payments to be paid between 2008 and 2017. Through fiscal year 2009, the State has received payments totaling $270.2 million. Fiscal year 2008 marked the first year of receipt of strategic payments, which were $14.4 million and are also included in the fiscal year 2009 total.

Pursuant to the Agreement, the expected settlement amounts are adjusted for inflation and the effect of any decreases in the sale of tobacco products to the base year. As of January 1, 2009, these have accounted for an 11.5 percent decrease. It remains difficult, therefore, to predict the amount of the future payments due from the tobacco settlement that will be received by the State.

The balance of the Tobacco Trust Fund investments at June 30, 2009, was $33.9 million and $34.5 million at the end of fiscal year 2008.

In fiscal year 2000, the Vermont Legislature established a Tobacco Litigation Settlement Fund ("Settlement Fund") to be administered by the State Treasurer and subject to further appropriations. In fiscal year 2009, $39.5 million from the settlement fund was directed to healthcare services (Medicaid; includes funds redirected to the Medicaid Global Commitment Fund). A total of $4.5 million was spent on programs in various departments for tobacco enforcement, prevention, and education programs. Additionally, $3.1 million funded substance abuse and youth protection programs in the Agency of Human Services. In fiscal year 2010, the legislature has appropriated $35.7 million for Medicaid health services; $4.5 million for enforcement, prevention, and education; and $3.3 million for substance abuse and youth protection programs. Any remainder of the settlement fund receipts is to remain in the fund for appropriation in fiscal year 2010. In fiscal year 2009, $1.7 million was transferred from the Tobacco Trust Fund to the Tobacco Litigation Settlement Fund per Act 192 section 4.004 of 2008. The balance of the Tobacco Trust Fund investments at June 30, 2009, was $33.9 million and $34.5 million at the end of fiscal year 2008.

Vermont's Expected and Actual Receipt of Tobacco Settlement Funds

Fiscal Year	Master Settlement Amount* ($millions)	Expected* ($ millions)	Actual* ($millions)
2001	$28.47	$28.47	$24.68
2002	34.18	34.18	30.92
2003	34.51	34.51	30.55
2004	28.80	28.80	25.82
2005	28.80	26.10	26.21
2006	28.80	24.50	24.06
2007	28.80	22.60	24.99
2008	29.37	39.50	39.91
2009	29.37	39.91	42.88

* Source: JFO. Master Settlement amounts shown are at time of initial settlement. Expected amount determined third quarter of each fiscal year unless noted. Actual excludes Settlement fund Account performance.

Short-Term Investments

The State Treasurer's Office manages the investment of the State's cash in its short-term investment program. The funds consist primarily of cash for operating needs to meet the daily needs of government. Given the investment horizon, the Treasurer's office ranks safety of principal as its first priority, followed by liquidity and return on investment. As noted in last year's report, the economic recession and credit crisis of 2008 and 2009 have impacted the entire spectrum

Vermont Veterans' Home

By legislative act in fiscal year 2001, the Vermont Veterans' Home was required to transfer its endowment fund to the State for administration by the State Treasurer. In the fall of 2001, the home transferred $455,441.85 into the trust to the State. The legislation allows the State Treasurer to invest these funds, if appropriate, with the long-term investments in the Investment Trust Account. The funds were invested with the State's short-term investments, until a spending policy for these funds was established by the Board of Trustees for the Vermont Veterans' Home. At the board's September 2002 meeting, a spending policy was adopted that allowed for transfer of the funds to a fund in the State's Trust Investment Account ("TIA"). Of the amount transferred, $400,000 was deposited in the TIA fund as of October 1, 2002. In November and December of 2002, the Vermont Veterans' Home received a bequest of $410,000 that was deposited into the TIA fund as a second, separately-named fund pursuant to the terms of the bequest. On July 1, 2004, an additional contribution of $75,000 was credited to this second fund. During fiscal year 2009, withdrawals from the Vermont Veterans' Home TIA funds totaled $40,000. As of June 30, 2008, the balance of the fund first contributed to the TIA was $471,195.28, and the balance of the second (later) fund was $560,313.70, for a combined total of $1,031,508.99.

of investments and has presented significant challenges. Many of the historically "safe" investments typically used by government treasury offices underwent significant upheaval and, over the past eighteen months, losses did occur at the state and local level outside of Vermont. The Office of the State Treasurer remains committed to meeting the cash needs of State operations while protecting the value of its assets, and approaches these responsibilities in a prudent, deliberate way.

Due to the weak economy, the Federal Reserve Board implemented some of the largest drops in monetary policy history, lowering its federal funds rate from 5.25 percent to a range between 0 percent and 0.25 percent. With the Federal Reserve Board holding the federal funds rate steady at a relatively low level, yields in money market portfolios have declined. We continue to invest in a more conservative portfolio rather than increasing risk by chasing return in leveraged or derivative instruments.

The short-term portfolio earned $3.09 million in interest income in fiscal year 2009 on average daily available balances of $198.9 million.

One aspect of the Treasurer's Office's risk management regarding short-term investments is collateralization of bank deposits. Although State statutes provide some requirement for the collateralization of deposits, they do not establish collateralization limits. It has been common practice for banks to provide deposit collateral required by the Treasurer's Office through pledged securities, at levels requested by the office. The Treasurer's Office periodically reviews and compares these collateralization levels to the practices of other states and large municipalities. During fiscal year 2008, the Treasurer's Office and the State's primary bank of record decided jointly to move to an irrevocable letter of credit with the Federal Home Loan Bank, which currently provides up to $175 million in coverage. In addition, the Treasurer's Office has made transaction account deposits with some banks that are guaranteed under the Federal Deposit Insurance Corporation's (FDIC) Transaction Account Guarantee Program (TAGP). Under the TAGP certain deposits are guaranteed by the FDIC above the standard FDIC insurance limits. As a matter of practice, CDs with the Bank in Vermont program have varying levels of collateralization, depending upon the bank, its assets, and capitalization levels, which are reviewed quarterly.

The short-term portfolio earned $3.09 million in interest income in fiscal year 2009 on average daily available balances of $198.9 million. Of this amount, $1,969,167 was credited to interest earning funds, and the balance of $1,124,505 remained in the general fund. The yield on the available cash in the portfolio was 1.56 percent for the year, which exceeded the average three-month Treasury Bill yield of 0.54 percent. The Treasurer's Office utilizes money market funds and in-state certificates of deposit, and solicits offerings from the institutional trading desks of a number of national and local brokers in order to achieve maximum rate of return and diversification in the portfolio.

Bank in Vermont Initiative

The Treasurer's Office continues to maintain its Bank in Vermont Program to invest State funds on a predictable basis through certificates of deposit (CDs) via a competitive bidding process in banks with branches in Vermont. The program is designed to be attractive to the wide range of banking institutions in Vermont, and is predicated on the belief that investing Vermont funds in Vermont, consistent with earning a competitive rate of return, is a good policy. A block of funds is set aside for the scheduled bid in specified time frames. The CDs may be short duration, or have longer maturities, depending on the yield curve and cash management requirements. Between its inception in August, 2004, and December, 2009, $570.25 million in CDs have been awarded. As of December 31, 2009, $5 million was invested in Bank in Vermont CDs of varying maturities with rates well above comparable maturity Treasury rates. During 2009, a total of $109.6 million in such CDs was issued. There have been no losses associated with this program.

Bank in Vermont: CDs Awarded and Outstanding through Dec. 31, 2009

Name	CDs AWARDED	CDs OUTSTANDING
	THROUGH 12/31/09	12/31/2009
CHITTENDEN BANK	19,350,000.00	
CITIZENS BANK	14,350,000.00	
CONNECTICUT RIVER BANK		
FIRST NATIONAL BANK OF ORWELL		
KEYBANK		
MASCOMA SAVINGS BANK		
MERCHANTS BANK	35,000,000.00	5,000,000.00
NATIONAL BANK OF MIDDLEBURY		
NORTHFIELD SAVINGS BANK		
PASSUMPSIC SAVINGS BANK		
PEOPLES TRUST CO OF ST. ALBANS		
RANDOLPH NATIONAL BANK	1,300,000.00	
TD BANK	38,400,000.00	
THE BANK OF BENNINGTON		
UNION BANK	1,200,000.00	
	109,600,000.00	5,000,000.00

Banks Pre-Qualified to Participate in Bank in Vermont through Dec. 31, 2009:

- Citizens Bank
- Chittenden Bank (a division of Peoples United Bank)
- Connecticut River Bank
- First National Bank of Orwell
- Key Bank
- Mascoma Savings Bank
- Merchants Bank
- National Bank of Middlebury
- Northfield Savings Bank
- Passumpsic Savings Bank
- Peoples Trust Company of St. Albans
- Randolph National Bank
- TD Banknorth Vermont TD Bank, N.A.
- The Bank of Bennington
- Union Bank

Unclaimed Property Division

Each fall, the Treasurer's Office distributes a list of new individual property through an insert published in Vermont's daily newspapers. Above, is the cover of the most recent publication. There were more than 6,500 names in the insert.

Unclaimed Property Division

(802) 828-2407
(800) 642-3191

Al LaPerle
Unclaimed Property Director

Nancy Scribner
Business Administrator

Linda Bouffard
Program Technician I

Kitty Bolduc
Program Technician I

Overview

Financial property becomes "unclaimed" after a business or non-profit entity loses contact with a customer for a period of years. The property is sent to the Treasurer's Office to protect the funds and centralize search efforts to locate property owners. The Unclaimed Property Division's primary goal is to reunite individuals with their unclaimed financial property. To accomplish this goal, the division uses a variety of tools. Foremost, the division must ensure that holders of the property file their annual unclaimed property report. Common sources of unclaimed property include old bank accounts; uncashed paychecks; money orders; service deposits; insurance policies; estates; safe deposit boxes; and stocks, bonds, and dividends.

UPDATES

Claims Processing

The Unclaimed Property Division acts as custodian to safeguard financial assets until they can be claimed by the rightful owner or heirs. The claims section paid more than 8,700 claims worth more than $5.6 million in fiscal year 2009, more than $1.2 million than last fiscal year. The average claim paid was $638. To reach owners of unclaimed property, we continue to capitalize on our past successes, such as publication of our annual list of names in daily newspapers; a spring advertising campaign; staffing a booth at the Champlain Valley Exposition; distribution of local listings to town clerks and legislators; and conducting other outreach events.

This year, we added two new processes to assist us in locating owners of unclaimed property. The first process was to cross-match our data with a database from the State Department of Taxes to locate the current addresses for unclaimed property owners. After we received the new addresses we sent the owners a letter, along with instructions on how to file their claim. We mailed more than 11,000

ACCOMPLISHMENTS IN 2009

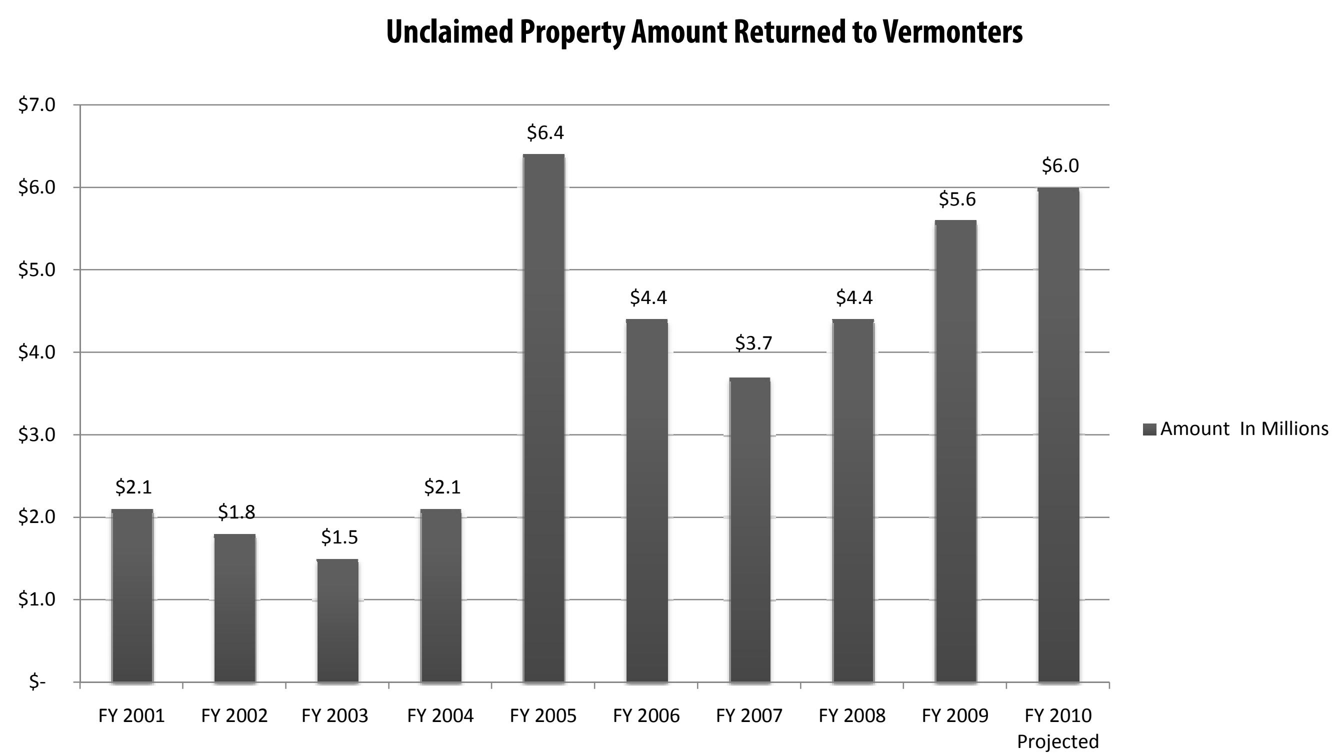
- **Paid 8,789 claimants more than $5.6 million - $1.2 million more than 2008.**
- **Implemented the initial stage of a technological upgrade to the unclaimed property system. That system currently contains a database of more than 182,000 properties valued at an estimated $47 million.**
- **Added 2,617 new holders to the unclaimed property system which have never reported unclaimed property in the past. Overall, holders of unclaimed property reported $8.4 million worth of unclaimed funds to the State in fiscal year 2009.**
- **In fiscal year 2009, there were 297,868 web searches for unclaimed property. We recently surpassed the division's one-day on-line claims search record by 437. On November 11, 2009, there were 14,859 single searches for unclaimed property. The previous one-day search total was 14,422 single searches on June 22, 2007.**

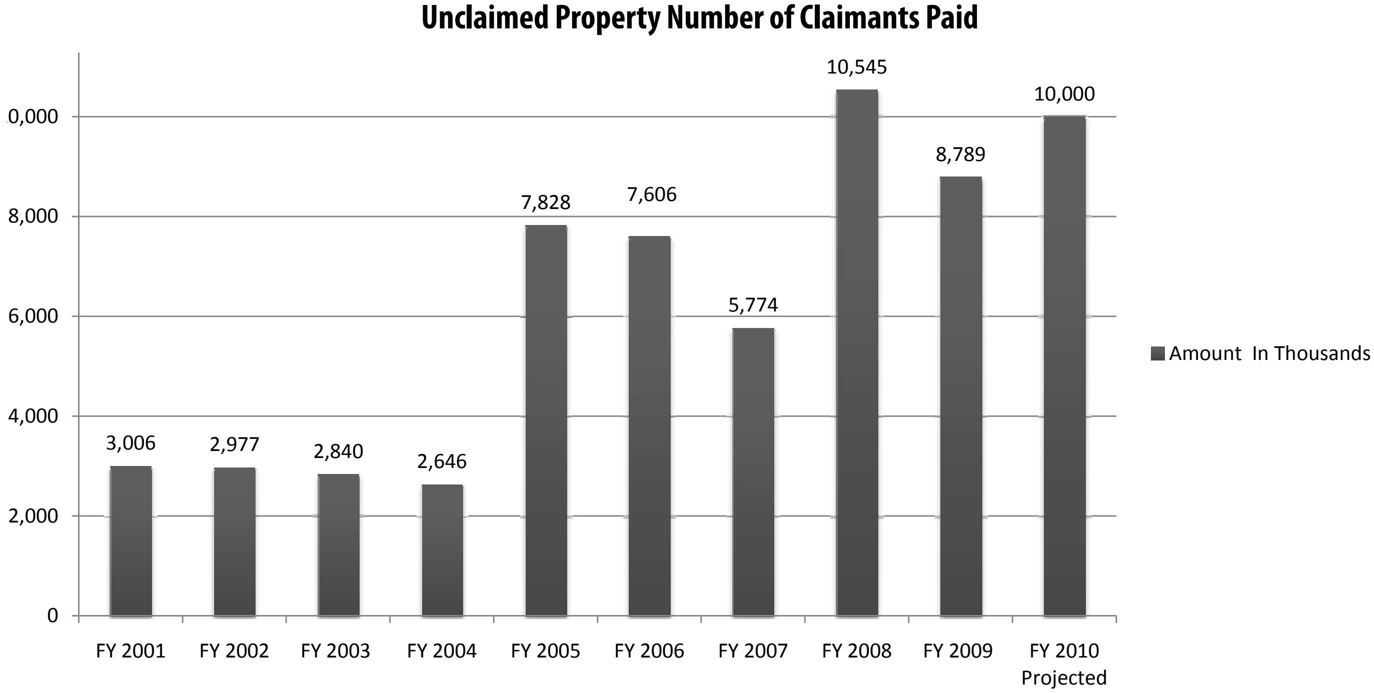
letters. The second process we implemented was to take new property that has been turned over to the State and send out a postcard to the owner informing them of their unclaimed property. We mailed approximately 3,000 postcards and have experienced very positive results. We intend to continue both of these very successful outreach activities.

To reach owners of unclaimed property, we continue to capitalize on our past successes, such as publication of our annual list of names in daily newspapers; a spring advertising campaign; staffing a booth at the Champlain Valley Exposition; distribution of local listings to town clerks and legislators; and conducting other outreach events.

In 2009, the division began a process to implement a comprehensive technological upgrade to the unclaimed property system. We believe this upgrade will enhance our outreach and our customer service response. This upgrade will eventually allow Vermonters to file a claim on line for their missing financial property. People can currently print a claim form off the web site, but they must still mail the document to the division and cannot file it electronically. This upgrade also will enable holders of unclaimed property to file their annual reports on line and upload those reports directly to the Treasurer's Office via a secure web portal. These initiatives will save time and money and will, ultimately, allow owners of unclaimed property to receive their funds more quickly.

Looking at fiscal year 2010, we are already off to a promising start in returning funds to Vermonters. From July 1 through December 1, 2009, the division had paid 3,994 claims, a 10 percent increase over the number of claims paid over the same time period the previous year. Claim information for fiscal year 2009 is shown in the charts below.



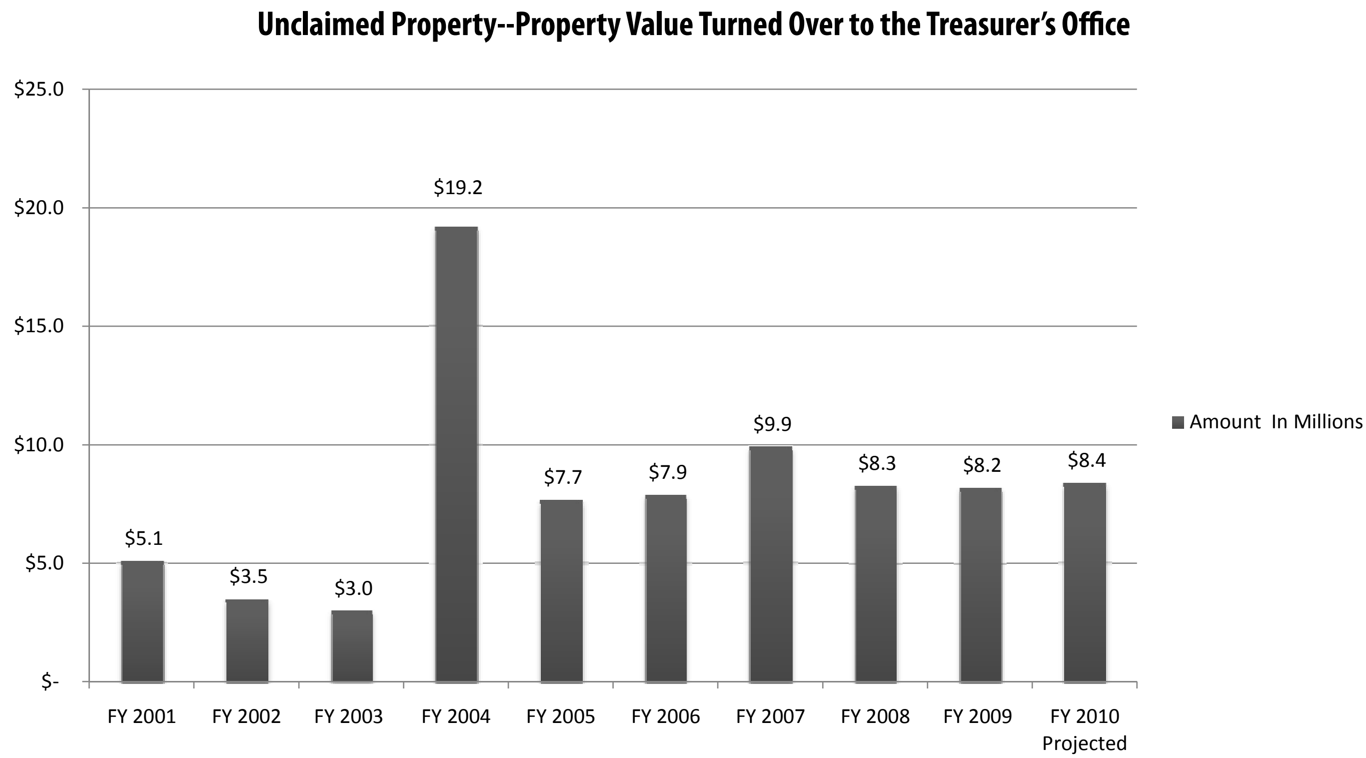


Reporting and Compliance

Banks, insurance companies, corporations, and the courts are among the many organizations known as holders that are required by law to report dormant accounts to the Unclaimed Property Division. Vermont's Unclaimed Property Law requires organizations to annually review their records and transfer accounts that have reached certain dormancy thresholds to the State Treasurer. The State Treasurer serves as custodian of the funds until they can be returned to their rightful owners. The State of Vermont is currently in possession of more than $47 million in unclaimed property belonging to approximately 182,000 individuals and organizations. Property becomes "lost" due to a company having no communication with the owner. This may be caused by an address change or change in marital status. In some cases, the owner dies and the heirs have no knowledge of the property. During fiscal year 2009, the State of Vermont received $8.4 million from holders of unclaimed property. Since January 1, 2009, the division added 2,617 new holders to the unclaimed property database.

The State of Vermont is currently in possession of more than $47 million in unclaimed property belonging to approximately 182,000 individuals and organizations.

The division uses several approaches to educate holders on their obligation to file their annual report. For example, the division participates in tax seminars conducted by various organizations at locations across the state. A division representative attends the seminar and will speak to attendees and staff an outreach table with information on the program. In fiscal year 2009, this approach gave us access to more than 500 potential holders of unclaimed property. We also have used four contract audit companies to assist us in the enforcement of the statute. These companies have enabled the division to touch base with a greater number of potential holders. Since the start of fiscal year 2010, 348 holders have surrendered more than $752,684 in financial property compared to 367 holders and $710,865 for the same period last year.



The division worked to take the unclaimed property database to Vermonters in a variety of settings. Above, Unclaimed Property Division Director Al LaPerle staffs an information table at a Lake Monsters game.

Treasury Operations Division

Treasury Operations Division: **(802) 828-2301**

John Booth
Treasury Operations Director

Dan Currier
Cash & Investments Manager

Ron Baldauf
Financial Specialist III

Lisa Gilman
Financial Specialist III

Becky Brockway
Financial Specialist II

Joanne Costantini
Financial Specialist II

Gayle Rowe
Financial Specialist II

Overview

The Treasury Operations Division processed approximately 1.5 million payments during the 2009 fiscal year. More than half of those payments were conducted electronically. The goal is to continue increasing the proportion of transactions that occur electronically. The division is responsible for the banking and cash management of more than $4 billion annually in both receipts and disbursements; the establishment and maintenance of the State's banking network; the disbursement of the State's warranted payments and debt service; the collection of certain receipts, including those related to Act 68; and the recording of accounting transactions associated with the above activities. The reconciliation of internal and external accounts comprises a major portion of the office's staff time, in addition to the proper reporting and recording on the State's books for financial reporting. In addition, the division is responsible for preparing financial statements and schedules for the annual audit of the State's books (as it relates to cash and investment disclosures), administering the Municipal Equipment Loan Fund, and assisting the Retirement Operations Division staff in the preparation of the pension trust fund financial statements. TD Bank, N.A. serves as the State's master banking contractor. Bank personnel and Treasury staff work continuously together to provide new and improved services and processes.

UPDATES

Reconciliations

The Treasurer's Office staff reconciles approximately 30 State core bank accounts. In fiscal year 2009, 80,190 deposits were processed to State accounts through a network designed to accelerate the collection of cash so that it may be

ACCOMPLISHMENTS IN 2009

- **Rolled out a "Vendor Portal" secure web site. This site allows State vendors that receive payments electronically to view payment information on line, reducing the number of requests for information from these vendors. As of October 31, 2009, approximately 170 vendors had created user accounts for this service. This is expected to expand significantly during the first year of operation.**

- **Completed a review of processes regarding tracking and follow-up of larger dollar vendor check payments, significantly reducing the number of stale-dated vendor check payments. This initiative helps ensure that vendor check payments are received and processed in a timely manner and allows us to encourage the use of direct deposit as an alternative payment method.**

- **Responded to more than 800 information requests received via the division's centralized e-mail account.**

- **Reconciliation of the State's core bank accounts was completed within 30 days of the monthly closing of the State's books, as has been the practice for nearly six consecutive years.**

used for operating needs or efficiently placed in short-term investments. On the disbursement side, 1,547,897 payments were processed, either through paper checks or electronic payments. Working cooperatively with all of the Treasury's business partners, we have been able to assure that the number and duration of reconciling items from user department entries remains low, and that reporting/review processes are in place to continually improve the accuracy and timeliness of financial reports and the supporting data.

Electronic Payments

The issuance of paper checks is labor-intensive and costly. Electronic payments reduce bank fees, printing costs, fraud, and postage, as well as staff time to reconcile bank accounts. Tracking of lost checks is time-consuming and can be largely eliminated through electronic payment processing. Time spent searching for cleared payments is eliminated. Bank fees related to "stop payments" are eliminated, as are the costs associated with re-issuing payments, and inconvenience to the payees. This past year, 1,502 check payments were reissued because the original check was lost or was never received by the payee.

The new vendor portal allows companies doing business with the State to view payment information on line. There are approximately 170 vendors who have created user accounts for this service.

The division is responsible for the banking and cash management of more than $4 billion annually in both receipts and disbursements.

One of the barriers to the use of electronic payments by vendors is the lack of payment remittance information received with the payment. The State currently issues and mails a remittance advice for each electronic payment. Of the more than 1.5 million payments processed during fiscal year 2009, approximately 57 percent were electronic transfers. During this fiscal year a "Vendor Portal" secure web site was rolled out. This web site allows vendors that receive payments electronically to view payment information online, which reduces the number of information requests received.

In November of 2009, 95.1 percent of monthly benefit payments to retired State employees were made via direct deposit. For the retired municipal employees, the percentage of monthly benefit payments via direct deposit was 89.2 percent and for retired teachers it was 96.2 percent. This is an increase from the November 2008 percentages of 93.4 percent-State, 87.7 percent-municipal, and 95.4 percent-teachers.

Act 68 Receipts

Notification and initial invoicing of the municipalities for the principal payment are completed by the Department of Education. Per statute, the Treasury Operations Division monitors the receipt of payments mandated by Act 68. In fiscal year 2009, all municipalities made their Act 68 principal payments.

As of December 8, 2009, all principal receivable for the payment due on December 1, 2009, had been collected. The Treasurer's Office has also billed interest, calculated at 8 percent per annum, for three municipalities that made principal payments after the December 1 due date. Subsequently, all of the interest payments were received. The Act 68 receipts approximate $81 million for the most recent semi-annual billing cycle.

Legislative Reporting Requirements

Brandon Training School/Vermont Veterans' Home

Section 23 of Act 62 of the Public Acts of 1995 specifies that the State Treasurer shall notify the chairs of the Senate and House Institutions committees upon receipt of monies from the sale of the Brandon Training School property, as well as certain federal receipts associated with the Vermont Veterans' Home. For fiscal year ending June 30, 2009, the State has timely received amounts due from the federal government associated with the Vermont Veterans' Home. There were no sales of property belonging to the Brandon Training School in fiscal year 2009.

Burma (Myanmar)

Act 13 of the Public Acts of 1999 specifies that the Treasurer shall implement the purposes of the Act by voting in favor of shareholder resolutions concerning individual companies doing business with the government of Burma. In addition, the Treasurer shall separately notify the company that Vermont wishes to convey its grave concerns regarding the company's economic ties to the government of Burma. The Treasurer complies with this Act through measures including mandating compliance through VPIC investment guidelines that must be observed by investment managers and by the proxy voting firm engaged by VPIC to vote its proxies. Proxy voting guidelines adopted by the three Vermont Retirement Systems and the Treasurer's office for U.S. domestic equity managers also specify manager voting compliance including support of labor standards in connection with a company's involvement in Burma, and reporting on Burmese operations and activities.

Credit Card Payments

The Treasurer's Office contracts with TD Bank Merchant Services Group, a division of TD Bank, N.A., to provide credit and bank card services. Acceptance of credit and debit card payments is broadly practiced in many agencies and departments as a method of payment of registration fees, licenses, penalties, fines, durable goods, park reservations, interest, and payment of taxes. Credit and debit card acceptance provides our customers, the citizens of Vermont, with a more convenient method of payment. In addition to public convenience, electronic processing of consumer and business purchases improves governmental cash flows, offers greater financial security, and reduces the overhead costs associated with the handling of currency.

The Vermont Information Consortium (VIC) provides credit card services to some Vermont agencies and departments that accept credit card and debit card payments for transactions conducted by cardholder via the internet. The Court Administrator has worked with VIC since February, 2007, to allow for the payment of fines and fees by credit card. In the fiscal year ending June 30, 2009, approximately 35,500 transactions were processed with almost $5.4 million collected in fines and fees. Of those transactions, approximately 34,000 were conducted by users over the internet, with the remaining transactions processed either in person at a District Court or over the phone. A convenience fee of $3.75 is currently charged to users of the service each time a person pays with their credit or debit card. In order to market the on-line credit card payment option for Judicial Bureau judgments, the Judiciary has added the web site address for the service to payment envelopes, the judgment form, and the collection notice. The judgment

MacBride Principles

Act 50 of the Public Acts of 1989 specifies that the State Treasurer and the Retirement Boards compile a list of corporations that conduct business in Northern Ireland in which the State Treasurer and Retirement Boards have invested funds. Notifications from external investment managers listing such businesses are due in the Treasurer's office on January 1 of each year, and these notifications are kept on file in the Treasurer's office. The Act further requires that the Treasurer and the boards of the trustees of the Vermont State Employees' Retirement System and the Vermont State Teachers' Retirement System shall support the MacBride Principles addressing worker equality and security issues through support of shareholder issues. The Treasurer's office and the trustees comply with Act 50 by mandating MacBride Principles compliance through Vermont Pension Investment Committee (VPIC) investment guidelines to be observed by investment managers and by the proxy firm engaged by VPIC to vote its proxies. Proxy voting guidelines approved by the three Vermont Retirement Systems and the Treasurer's office for U.S. domestic equity managers also specify manager voting compliance with MacBride principles.

Credit Card Accounts Summary

DEPARTMENT	TOTAL SALES	TOTAL FEES
VT Dept. of Liquor Control	17,932,372.24	396,463.63
VT Dept. of Motor Vehicles	15,015,637.84	263,185.29
VT Dept. of Taxes *	4,288,999.35	9,066.93
VT Dept. of Forest, Parks & Recreation	2,600,400.51	58,106.85
VT Dept of Fish & Wildlife	1,204,854.35	23,725.92
VT Life Magazine	244,175.99	5,798.44
VT Secretary of State	1,423,985.00	39,923.37
VT Judicial / Courts	5,892,162.13	13,299.47
VT Center for Crime Victims / Restitution Unit	194,958.00	3,669.69
VT Dept of Health	171,310.98	3,948.93
VT Dept. of Environmental Conservation	12,471.50	341.73
VT Dept. of Historic Preservation / Historic Sites	126,050.62	4,385.22
VT Dept. of Child & Family Services	703,285.00	16,308.50
VT Dept. of Public Safety **	172,023.50	0.00
VT Agency of Transportation / Contract Administration	133.00	138.34
TOTAL	49,982,820.01	838,362.31

* This represents card processing fees paid by the Department of Taxes for this reporting period. Certain taxpayers using credit cards to make payments to the department pay a convenience fee, which offset the card processing fees for those payments.

** Cardholders using this service pay a convenience fee, which offset all of the card processing fees for this service for this reporting period.

form and the collection notice also include a tear-off credit card payment stub that can be mailed.

Financial Literacy Trust Fund

The legislature authorized the establishment of a trust fund to finance financial literacy in Vermont. According to the legislation, "the purpose of the fund is to promote the adoption of fiscally sound money management practices by Vermonters through education and outreach efforts that raise awareness of the need for and benefits of practicing such skills; and to create opportunities to build and encourage the development of new financial literacy activities and educational products for Vermont citizens." The Treasurer is authorized to collect money from a variety of sources to fund these activities. For fiscal year 2009, the fund received deposits of $5,400 earning $35.53 in interest. There was $3,442.30 expended from the trust fund during fiscal year 2009. Expenditures from the fund supported a statewide financial literacy poster contest; allowed for implementation of a new MoneyEd initiative that included production and distribution of an educational DVD on personal money management; and enabled the Treasurer's Office to organize the first statewide "Reserve Cup" team competition to challenge high school students to learn more about finances and economics. More detail on these programs is provided in the financial literacy section of this annual report.

Survivors of Emergency Personnel

Originally established by the legislature in 2002 as the Firefighters' Survivors Benefit Fund, this fund was expanded during the 2005 legislative session to include not only firefighters, but ambulance service, emergency medical, first responder service and volunteer personnel. A review board administers the grant of a one-time monetary benefit to the survivor or survivors of emergency personnel employed by or who volunteer for the state of Vermont, a county or municipality of the state, or a nonprofit entity which provides services in the state, who die in the line of duty or of an occupational-related illness. During the past year payments have been made related to the deaths of two emergency personnel in the line-of-duty. In addition, $50,000 was transferred out of this fund during fiscal year 2009. As of November 30, 2009, this fund has assets of $86,647.90.

Technology Update

Technology Services

The Technology Services Division is committed to providing programming and technical support services to the Treasurer's Office. Office personnel in this area provide support to the entire range of software and hardware facilitating the operations of the office, including banking reconciliation software, check and EFT issuance, unclaimed property, and the various programs supporting the retirement services for the State's approximately 44,000 active, vested, and retired members.

UPDATES

The Technology Services staff continued to implement important upgrades to the office's infrastructure to improve the speed and dependability of its systems during 2009. Listed below are our accomplishments.

- **The implementation of the Treasurer's Office web-based Vendor Advice Portal was completed in the spring of 2009. This new functionality allows vendors to more quickly reconcile payments. The Vendor Portal promotes the use of electronic payments over the more costly check payment process.**

- **The server hardware at both our main data center in Montpelier and our disaster recovery site in Barre was upgraded to the latest generation of server hardware technology to improve performance, reliability and disaster recovery.**

- **The Unclaimed Property system was successfully upgraded to the latest version that fully utilizes current technologies. This technology platform will allow us to improve our internal processes and more easily deploy self-service functions via the web.**

- **The Treasurer's Office web site was redesigned and moved onto the Vermont State portal managed by the Vermont Information Consortium. It is a flexible system that has allowed us to build in some distinct design appearances that allow people to know they are on the Treasurer's Office web site and not just a generic State page. Utilizing the portal enables us to have 24-hour, seven-days-a-week web security and back-up for our site, and will take care of any past challenges we have had regarding access should a server go down. The new portal system also enables us to more easily update our web content.**

- **VPAS (Vermont Pension Administration System) has achieved a major milestone by implementing Pension Payroll starting with the November 2009 payments. The active member maintenance and employee reporting functions are part of the final phase that is targeted for completion in 2010.**

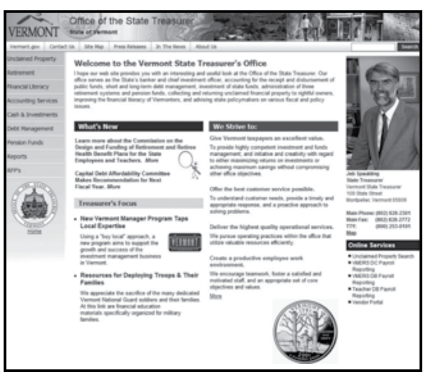
We will continue working closely with various Treasurer's Office operations staff and other departments to enhance existing services, such as improvements to our existing infrastructure, and planning for a comprehensive check-printing solution.

Technology Services
(802) 828-2498

Ram Verma
Technology Services Director

Lane Safford
Network Administrator II

Karen Willey
Systems Developer III



The Treasurer's Office web site was migrated to the Vermont State portal in 2009. The new site went live on October 19. In the first three months since the site went live, an estimated 70,601 unique visitors have utilized the web site.

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HISTORICAL SUMMARY OF OPERATIONS: *Pension Fund Operations*

State Employees' Retirement System -- Summary of Operations

Category	2003	2004	2005	2006	2007	2008	2009
SOURCES OF FUNDS							
Employee Contributions	$ 12,171,186	$ 13,716,264	$ 15,112,105	$ 14,561,467	$ 15,456,691	18,614,102	25,134,235
Employer Contributions	24,394,933	26,645,619	36,493,435	36,866,451	39,297,002	39,179,823	22,148,754
Other Income	813,168	695,397	777,792	1,171,516	205,321	169,984	1,041,870
Investment Income (Reduction)	40,435,216	138,426,552	90,452,723	115,146,415	192,625,279	(84,156,254)	(242,976,381)
APPLICATION OF FUNDS							
Retirement Benefits	41,614,187	44,637,116	48,893,673	53,435,617	58,859,659	64,060,488	70,043,119
Refunds	923,964	1,171,957	1,402,481	1,351,911	1,526,140	1,414,144	1,403,995
Health/Life Insurance Expenses	9,916,398	9,236,526	11,329,269	11,590,588	13,541,092	16,371,373	0
Administrative Expenses	971,394	659,447	1,255,852	1,329,081	511,435	1,254,577	1,219,287
Other Expenses	369,383	617,658	635,618	668,929	344,719	631,321	477,966
Addition (Reduction) to Net Assets Held In Trust for Pension Benefits	$ 24,019,177	$ 123,161,128	$ 79,319,162	$ 99,369,723	$ 172,801,248	$ (109,924,248)	$ (267,795,889)

Teachers' Retirement System -- Summary of Operations

Category	2003	2004	2005	2006	2007	2008	2009
SOURCES OF FUNDS							
Employee Contributions	$ 18,820,703	$ 21,088,345	$ 21,158,452	$ 21,884,140	$ 22,533,479	22,918,798	20,937,686
Employer Contributions	20,446,282	24,446,282	24,446,282	24,446,282	37,341,609	39,549,097	35,960,934
Other Income	438,166	267,330	373,705	1,180,606	2,093,219	1,628,242	3,754,020
Investment Income (Reduction)	52,506,838	166,325,045	115,058,694	130,835,585	244,437,213	(110,019,634)	(307,382,559)
APPLICATION OF FUNDS							
Retirement Benefits	50,409,313	55,246,342	60,147,731	66,272,471	74,368,306	82,157,642	89,825,986
Refunds	1,109,174	711,806	1,104,278	1,290,197	1,625,140	1,280,715	1,420,776
Health/Life Insurance Expenses	6,634,738	8,279,332	10,167,601	11,233,854	13,040,783	15,081,847	16,421,176
Administrative Expenses	763,527	805,495	1,052,772	1,679,883	817,052	866,473	1,249,774
Other Expenses	702,568	543,746	682,438	580,403	203,444	542,665	606,434
Addition (Reduction) to Net Assets Held In Trust for Pension Benefits	$ 32,592,669	$ 146,540,281	$ 87,882,313	$ 97,289,805	$ 216,350,795	$ (145,852,839)	$ (356,254,065)

Municipal Retirement System -- Summary of Operations

Category	2003	2004	2005	2006	2007	2008	2009
SOURCES OF FUNDS							
Employee Contributions	$ 5,000,479	$ 6,507,268	$ 7,404,119	$ 8,744,718	$ 9,769,882	9,906,709	9,557,973
Employer Contributions	5,707,184	7,114,813	8,058,810	7,926,436	8,535,396	0	8,008,862
Other Income	17,855,452	2,125,294	298,475	228,746	206,101	124,132	1,321,919
Investment Income (Reduction)	2,630,247	27,271,821	18,165,861	27,697,371	46,637,360	(19,472,654)	(56,937,342)
APPLICATION OF FUNDS							
Retirement Benefits	4,929,747	5,694,080	6,418,097	7,120,325	7,969,703	9,064,725	10,228,263
Refunds	639,170	1,110,243	1,140,245	1,102,940	1,389,583	1,143,397	1,223,465
Health/Life Insurance Expenses	-	-	-	-	-	0	0
Administrative Expenses	118,038	151,228	367,810	439,983	687,382	623,619	798,458
Other Expenses	546,692	668,624	423,937	1,101,883	560,473	506,817	588,899
Addition (Reduction) to Net Assets Held In Trust for Pension Benefits	$ 24,959,715	$ 35,395,021	$ 25,577,176	$ 34,832,140	$ 54,541,598	$ (20,780,371)	$ (50,887,673)

State Employees' Retirement System (OPEB) -- Summary of Operations

Category	2008*	2009
	SOURCE OF FUNDS	
Employee Contributions		0
Employer Contributions	1,444,757	19,893,129
Other Income		0
Investment Income (Reduction)	7,886	86,454
	APPLICATION OF FUNDS	
Retirement Benefits		0
Refunds		0
Health/Life Insurance Expenses		17,894,518
Administrative Expenses		0
Other Expenses		0
Addition (Reduction) to Net Assets Held In Trust for Pension Benefits	$ 1,452,643	$ 2,085,065

*** In 2008, changes made to the Government Accounting Standard Board requirements mandated that institutions report the future cost of other post-employment benefits (OPEB).**

STATE OF VERMONT: *Pension Trust Funds—Combining Statements of Plan Net Assets—6/30/2009*

	Defined Benefit Plans			Defined Contribution Plans			Other Postemployment Benefits Funds			
	Vermont State Retirement Fund	State Teachers' Retirement Fund	Vermont Municipal Employees' Retirement Fund	Vermont State Defined Contribution Fund	Single Deposit Investment Account Fund	Vermont Municipal Employees' Defined Contribution Fund	Vermont State Postemployment Benefits Trust Fund	Vermont Municipal Employees' Health Benefit Fund	Eliminations	Total
Assets:										
Cash and short term investments	$ 2,232,186	$ 2,148,484	$ 1,103,898	$ 181,726	$ 3,521,761	$ 62,883	$ 718,975	$ 127,398	$ -	$ 10,097,311
Receivables:										
Contributions - current	4,315,714	2,462,424	2,364,080	145,915	-	20,066	-	-	-	9,308,199
Contributions non-current	-	-	6,546,347	-	-	-	-	-	-	6,546,347
Interest and dividends	3,793	2,916	393,481	-	649,302	-	-	-	-	1,049,492
Investments sold	-	-	-	-	1,236,325	-	-	-	-	1,236,325
Due from other funds	35,635	-	33,887	-	-	-	485,680	-	(69,522)	485,680
Other	-	310,438	-	-	-	-	-	-	-	310,438
Total receivables	4,355,142	2,775,778	9,337,795	145,915	1,885,627	20,066	485,680	-	(69,522)	18,936,481
Investments at Fair value:										
Pooled investments	1,007,287,404	1,135,514,287	264,546,223	-	-	-	-	-	-	2,407,347,914
Fixed income	-	23	-	-	76,456,190	-	3,068,680	-	-	79,524,893
Equities	-	388	-	-	30,840	-	1,249,660	-	-	1,280,888
Real estate and venture capital	1,306,170	3,272,912	1,166,402	-	-	-	-	-	-	5,745,484
Mutual funds	-	-	-	32,472,751	-	11,607,167	225,587	8,910,561	-	53,216,066
Total investments	1,008,593,574	1,138,787,610	265,712,625	32,472,751	76,487,030	11,607,167	4,543,927	8,910,561	-	2,547,115,245
Prepaid expenses	-	1,363,987	-	10,564	-	-	-	-	-	1,374,551
Capital Assets:										
Construction in progress	1,152,139	1,322,164	359,443	-	-	-	-	-	-	2,833,746
Capital assets being depreciated:										
Equipment	77,261	89,790	41,763	-	-	-	-	-	-	208,814
Less accumulated depreciation	(44,683)	(51,933)	(24,102)	-	-	-	-	-	-	(120,718)
Total capital assets	1,184,717	1,360,021	377,104	-	-	-	-	-	-	2,921,842
Total assets	**1,016,365,619**	**1,146,435,880**	**276,531,422**	**32,810,956**	**81,894,418**	**11,690,116**	**5,748,582**	**9,037,959**	**(69,522)**	**2,580,445,430**
Liabilities:										
Payable for investments purchased	-	-	-	-	2,194,430	-	-	-	-	2,194,430
Accounts payable	1,547,700	1,225,587	296,000	37,540	-	196	-	-	-	3,107,023
Retainage payable	119,937	144,179	62,993	-	-	-	-	-	-	327,109
Due to other funds	-	-	-	35,635	-	33,887	-	-	(69,522)	-
Total liabilities	**1,667,637**	**1,369,766**	**358,993**	**73,175**	**2,194,430**	**34,083**	**-**	**-**	**(69,522)**	**5,628,562**
Net assets held in trust for employees' pension and other postemployment benefits	**$ 1,014,697,982**	**$ 1,145,066,114**	**$ 276,172,429**	**$ 32,737,781**	**$ 79,699,988**	**$ 11,656,033**	**$ 5,748,582**	**$ 9,037,959**	**$ -**	**$ 2,574,816,868**

STATE OF VERMONT: *Pension Trust Funds—Combining Statements of Changes in Plan Net Assets—Fiscal Year Ended 6/30/2009*

	Defined Benefit Plans			Defined Contribution Plans			Other Postemployment Benefits Funds			
	Vermont State Retirement Fund	State Teachers' Retirement Fund	Vermont Municipal Employees' Retirement Fund	Vermont State Defined Contribution Fund	Single Deposit Investment Account Fund	Vermont Municipal Employees' Defined Contribution Fund	Vermont State Postemployment Benefit Trust Fund	Vermont Municipal Employees' Health Benefit Fund	Eliminations	Total
Additions :										
Contributions										
Employer - pension benefit	$ 25,134,235	$ 19,260,934	$ 8,008,862	$ 1,520,354	$ -	$ 686,245	$ -	$ -	$ -	$ 54,610,630
Employer - healthcare benefit	-	16,700,000	-	-	-	-	19,893,129	1,944,109	-	38,537,238
Plan member	22,148,754	20,937,686	9,557,973	657,129	-	640,732	-	-	-	53,942,274
Transfers from other pension trust funds	246,476	453,488	244,624	74,926	-	42,193	-	-	(1,061,707)	-
Transfers from non-state systems	795,394	1,911,648	1,077,295	-	-	-	-	-	-	3,784,337
Medicare part D drug subsidy	-	1,388,884	-	-	-	-	-	-	-	1,388,884
Total contributions	**48,324,859**	**60,652,640**	**18,888,754**	**2,252,409**	**-**	**1,369,170**	**19,893,129**	**1,944,109**	**(1,061,707)**	**152,263,363**
Investment Income:										
Net appreciation (depreciation) in fair value of investments	(796,772)	472,870	394,805	(7,689,824)	(2,545,458)	(2,831,581)	(93,081)	(873,548)	-	(13,962,589)
Income (loss) from pooled investments	(240,509,484)	(306,111,171)	(57,426,538)	-	-	-	-	-	-	(604,047,193)
Dividends	-	-	-	1,233,497	6,703	381,195	37,850	-	-	1,659,245
Interest income	36,702	85,349	795,048	2,181	4,185,836	759	141,685	15,604	-	5,263,164
Securities lending income	2,290,357	2,683,170	461,935	-	730	-	-	-	-	5,436,192
Other income	586,770	799,619	102,263	31	5,537	31	-	-	-	1,494,251
Total investment income (loss)	**(238,392,427)**	**(302,070,163)**	**(55,672,487)**	**(6,454,115)**	**1,653,348**	**(2,449,596)**	**86,454**	**(857,944)**	**-**	**(604,156,930)**
Less Investment Expenses:										
Investment managers and consultants	(4,033,847)	(4,666,821)	(1,139,931)	-	(331,667)	-	-	(50,299)	-	(10,222,565)
Securities lending expenses	(550,108)	(645,574)	(124,924)	-	-	-	-	-	-	(1,320,606)
Total investment expenses	**(4,583,955)**	**(5,312,395)**	**(1,264,855)**	**-**	**(331,667)**	**-**	**-**	**(50,299)**	**-**	**(11,543,171)**
Net investment income (loss)	**(242,976,382)**	**(307,382,558)**	**(56,937,342)**	**(6,454,115)**	**1,321,681**	**(2,449,596)**	**86,454**	**(908,243)**	**-**	**(615,700,101)**
Total additions	**(194,651,523)**	**(246,729,918)**	**(38,048,588)**	**(4,201,706)**	**1,321,681**	**(1,080,426)**	**19,979,583**	**1,035,866**	**(1,061,707)**	**(463,436,738)**
Deductions:										
Retirement benefits	70,043,119	89,825,986	10,228,263	2,185,464	6,195,782	472,754	-	-	-	178,951,368
Other post employment benefits	-	16,421,176	-	-	-	-	17,894,518	645,233	-	34,960,927
Refunds of contributions	1,403,995	1,420,776	1,223,465	-	-	-	-	-	-	4,048,236
Death claims	177,194	397,607	246,351	-	-	-	-	-	-	821,152
Transfers to other pension trust funds	300,772	208,828	552,107	-	-	-	-	-	(1,061,707)	-
Depreciation	18,045	20,976	9,703	-	-	-	-	-	-	48,724
Operating expenses	1,201,242	1,228,798	579,196	36,170	-	66,532	-	-	-	3,111,938
Total deductions	**73,144,367**	**109,524,147**	**12,839,085**	**2,221,634**	**6,195,782**	**539,286**	**17,894,518**	**645,233**	**(1,061,707)**	**221,942,345**
Change in net assets	**(267,795,890)**	**(356,254,065)**	**(50,887,673)**	**(6,423,340)**	**(4,874,101)**	**(1,619,712)**	**2,085,065**	**390,633**	**-**	**(685,379,083)**
Net assets held in trust for employees' pension and other postemployment benefits:										
July 1	**1,282,493,872**	**1,501,320,179**	**327,060,102**	**39,161,121**	**84,574,089**	**13,275,745**	**3,663,517**	**8,647,326**	**-**	**3,260,195,951**
June 30	**$ 1,014,697,982**	**$ 1,145,066,114**	**$ 276,172,429**	**$ 32,737,781**	**$ 79,699,988**	**$ 11,656,033**	**$ 5,748,582**	**$ 9,037,959**	**$ -**	**$ 2,574,816,868**

HIGHER EDUCATION TRUST FUND: *Annual Report—September 15, 2009*

TO: Commission on Higher Education Funding

FROM: Jeb Spaulding, State Treasurer

RE: Annual Report on the Higher Education Trust Fund

DATE: September 15, 2009

I am pleased to present the State Treasurer's tenth annual report on the Higher Education Trust Fund. This Fund was established in the Office of the State Treasurer by the 1999 General Assembly to provide non-loan financial aid to Vermont students attending the University of Vermont, the Vermont State Colleges, and other Vermont post-secondary institutions (16 V.S.A. § 2885).

During Fiscal Year 2009, the Higher Education Trust Fund dollar weighted investment return was 2.40% gross of fees. This return compares to the Barclays (formerly Lehman) Aggregate Bond Index return of 6.06% and to the S&P 500 Stock Index return of -26.21% for the same period, and exceeds the Fund's target allocation index rate (that is, the rate of return that would have been realized if 30% of the Fund was invested in the S&P 500 Index, and 70% in the Barclays Aggregate) of -1.19%. A detailed discussion of the Fund's performance is included in this report.

5% Distribution from Fiscal Year 2009

The statute provides that in August of each fiscal year, the State Treasurer is to withdraw 5% of up to a 12-quarter moving average of the Fund's assets and divide the amount equally among the University of Vermont, the Vermont State Colleges, and the Vermont Student Assistance Corporation. The amount appropriated, however, cannot exceed an amount that would bring the Fund balance below total contributions to principal (total principal contributions through June 30, 2009 have been $15,879,896; see Chart #1 for a detail of appropriation amounts by fiscal year).

The 5% distribution available this year is $872,676.09 in total, or $290,892.03 each for UVM, VSC, and VSAC. This amount represents a 12.2% increase over the distribution made following Fiscal Year 2008 of $259,215.90 for each institution (see Appendix A for quarterly market values and distributions for Fiscal Year 2009).

2% Distribution from Fiscal Year 2008

16 V.S.A. § 2885 further provides that during the first quarter of each fiscal year, the Commission on Higher Education Funding may authorize the State Treasurer to make an additional amount equal to up to 2% of the Fund's average assets available to UVM and the Vermont State Colleges for the purpose of creating or increasing a permanent endowment fund. Similar to the 5% distribution, the amount appropriated cannot exceed an amount that would bring the Fund balance below total contributions to principal. Further, each institution is required to match the appropriation by raising private donations of at least twice the appropriated amount, to certify to the Commissioner of Finance and Management that it received private donations in the requisite amount, and that the funds will be used to create or increase a permanent endowment at the respective institution.

At its meeting last year, the Commission authorized this 2% appropriation in the amount of $311,059.08, or $155,529.54 each for distribution to UVM and the Vermont State Colleges, dependent upon a finding by the Commission that the terms of this appropriation have been met. Each of these institutions is in the process of establishing the required certification. However, owing to the Fund's relatively small positive return in FY 2009, the Fund can only distribute $298,227.18, or $149,113.59 (approximately 96% of the authorized amount) each to UVM and the Vermont State Colleges, and still maintain the statutorily-required $15,879,896 balance equal to contributed principal.

After payments of $872,676.09 and $298,227.18, the balance in the Fund at the end of FY 2009 totals $15,879,896. An accounting of the Fund balances is provided below:

Ending balance FY 2008		$17,917,152.20
Contributions received FY 2009		0.00
Opening balance FY 2009		17,917,152.20
Distribution September 2008		(968,671.55)
Income earned FY 2009		762,760.48
Appreciation (Depreciation) FY 2009		(594,047.48)
Fees and Other Charges FY 2009		(66,394.70)
Balance June 30, 2009		17,050,798.96
5% of 12-Quarter Moving Average as of June 30, 2009		(872,676.09)
Distributions:	University of Vermont	(290,892.03)
	Vermont State Colleges	(290,892.03)
	Vermont Student Assistance Corp.	(290,892.03)
2% Income Available for Endowments from FY 2008		(298,227.18)
Balance after distributions		15,879,895.69

Total contributions as of June 30, 2009	15,879,895.69
2% Income Available for Endowments from FY 2009 (requires institutional match in FY 2010)	$349,070.43

2% Distribution for Fiscal Year 2009

All principal contributions to the Fund through June 30, 2009 total $15,879,895.69, which also represents the minimum balance that must be maintained in the Fund (this amount does not include a total of $1,573,457 of contributions received on June 30, 2009, which will be applied to the starting principal balance for FY 2010).The 2% distribution proposed for this year of $349,070.43 would leave a balance of $15,530,825.26 excluding contributions to be received, and the 5% distribution following FY 2010, and any gains from investment activity in FY 2010. If the Commission authorizes this distribution, each institution's share will be $174,535.22 with a required match to be raised by each entity in FY 2010 of $349,070.43. The attached Chart #2 provides a graphical depiction of authorized distributions, including this 2% distribution subject to Commission approval.

Fund Balances, Performance, and Additional Information

I have attached a spreadsheet as Appendix B that shows the total return of the entire Trust Investment Account, of which the Higher Education Trust Fund at $17,050,798.96 (prior to cash distributions to be made in FY 2010) comprises approximately 29%. The Tobacco Trust Fund comprises 57% of the account, or $33,863,923, and the remaining 14% is made up of eight small trusts that total $462,038.46, the ANR Stewardship Fund at $703,195.88, two Veterans' Home trusts totaling $1,031,509, the Fish and Wildlife Trust Fund at $1,283,566 and a State Employees' retirement benefits trust of $4,801,431. Chart #3 displays the relative share of the Higher Education Trust Fund compared to the entire Fund, and chart #4 identifies the major asset classes in the portfolio and their performance over the past nine years.

As noted in Chart #5, assets increased significantly in FY 2007 due to receipt of funds raised by the Estate Tax in the amount of $5,223,449.94 and a $600,000 contribution from the State's unclaimed property fund as a result of legislation proposed by the Treasurer in FY 2006. Both of these amounts were derived from FY 2006 and were received into the Fund in FY 2007. Assets decreased slightly in FY 2008 as a result of investments returns in FY 2008 being less than distributions made in FY 2008 as well as the small amount of contributions received in FY 2008. Finally, in FY 2009, assets decreased more significantly owing to larger distributions coupled with virtually flat overall portfolio returns.

Fixed income investments have been the principal source of total return over the life of the Fund due to a combination of Fund asset allocation and market forces. However, in both FY 2006 and FY 2007 equity investments provided the majority of the contribution to the Fund's investment performance based on favorable equity market conditions in those years and a combined above benchmark performance by the equity managers.

In both FY 2008 and FY 2009, the Fund achieved a modest positive investment return in spite of the worst financial market conditions since the Great Depression. This was due to the conservative asset allocation in favor of fixed income securities, significant outperformance of the Barclay's Aggregate fixed income benchmark by both fixed income investment managers, and significant outperformance of the S&P 500 Index benchmark by one of the equity managers, Prentiss Smith & Co. The other equity manager, Hanson Investment Management, slightly underperformed the benchmark in 2009, but has otherwise substantially and consistently outperformed the benchmark historically.

In FY 2008, the Access Capital Strategies Community Investment Fund was added to the Trust Investment Account as a fixed income manager. This fund invests in very high grade housing and other bonds with an amount approximately equal to the initial investment of $2,500,000 funding principally housing in Vermont. For FY 2009, Access Capital returned 8.72% gross of fees, or 266 basis points (2.66%) in excess of its benchmark, and also returned very similar overall performance to NL Capital Management, the other fixed-income manager. Thus, the assets invested with Access Capital are meeting goals of preservation of capital and investment return along with providing benefits to Vermonters.

The asset allocation of the Fund at June 30, 2009, comprised 30.6 % equities and 69.4% fixed income securities, versus 26.8% equities and 73.2% fixed income securities, respectively, on June 30, 2008. Currently, allocations of contributions and sources of distributions in the Trust Investment Account are used to target a 30%-to-70% ratio in favor of fixed income securities. Given that the current allocation is very close to the target, subsequent contributions and minor annual rebalancing will be sufficient to "tune" this ratio to a more precise balance. This asset allocation addresses joint investment objectives of investment return and capital preservation, and has provided an overall positive return despite almost unprecedentedly poor market conditions.

In summary, while the investment performance of the Trust Investment Account once again exceeded its target return, unfavorable equity market conditions created a return below a level fully supporting this year's distributions. Going forward, and especially in the coming Fiscal Year, distributions will depend on the ongoing performance of the Fund, will require continued monitoring of the Fund's investment performance, and may warrant ongoing consideration of the optimal asset allocation given the recent and substantial changes to the investment marketplace.

Please feel free to contact me if you have any questions or concerns regarding this report.

cc: James Reardon, Commissioner of Finance & Management
Donna Russo-Savage, Legislative Council

APPENDIX A: *Quarterly Market Values—Period Ending June 30, 2009*

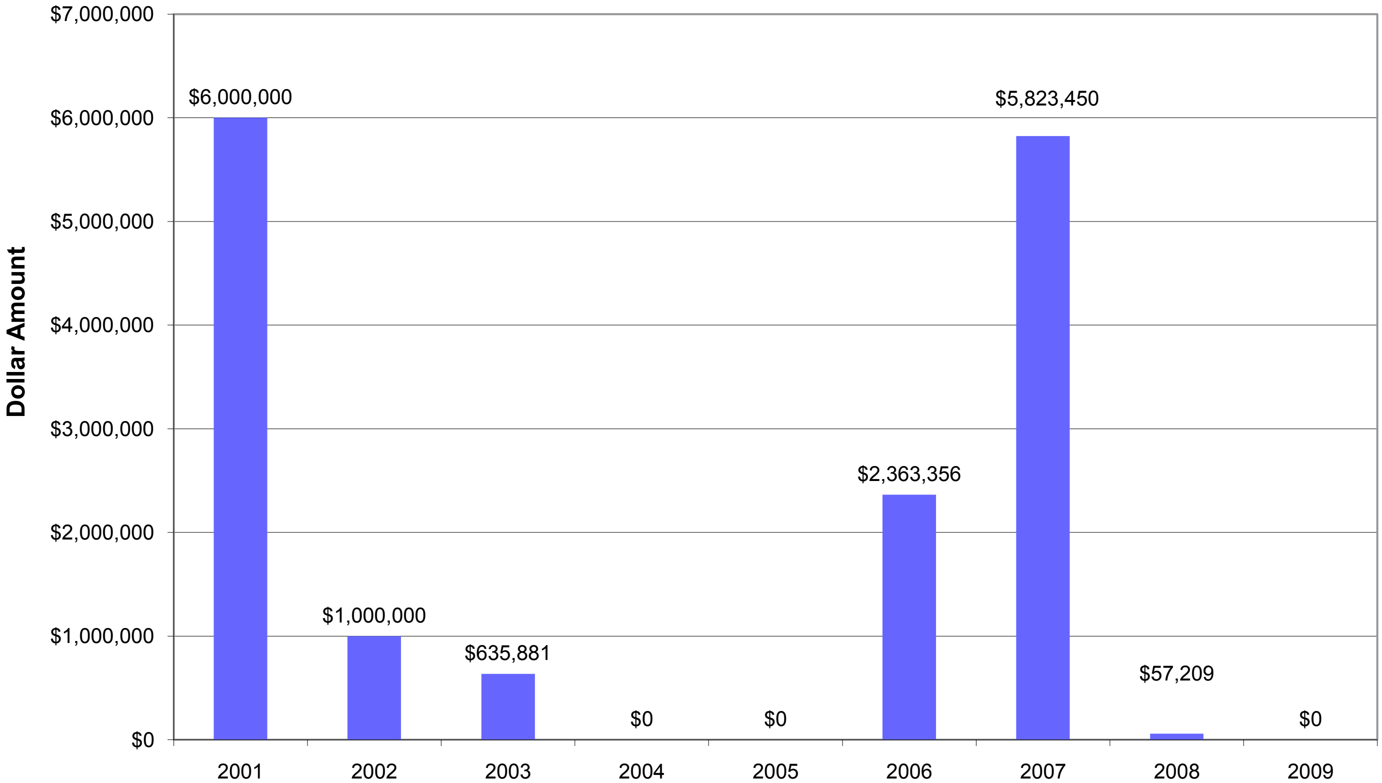
	Balance	Balance	Balance	Balance		
	9/30	12/31	3/31	6/30		
Education Trust						
FY2007	$16,853,847.32	$17,407,882.23	$17,896,475.61	$18,269,599.72		
FY 2008	$17,827,605.83	$18,164,200.03	$18,010,390.14	$17,974,360.85		
FY2009	$16,966,384.87	$16,320,715.01	$16,700,000.00	$17,050,798.96		
Twelve Quarter Average	**$17,453,521.71**					
5% Distribution 2009	**$872,676.09**					
VSAC		$290,892.03		Contributions		
UVM		$290,892.03				
VSC		$290,892.03		2001	$6,000,000.00	
				2002	$1,000,000.00	
2% FY2008 (Projected)	**$311,059.08**			2003	$635,881.49	
UVM		$155,529.54		2004	$0.00	
VSC		$155,529.54		2005	$0.00	
				2006	$2,363,355.61	
2% FY2008 (Actual)	**$298,227.18**			2007	$5,823,449.94	
UVM		$149,113.59		2008	$57,208.65	
VSC		$149,113.59		2009	$0.00	
				Total*	**$15,879,895.69**	
Balance after Distributions	**$15,879,895.69**					
2% FY2009	$349,070.43					
UVM		$174,535.22				
VSC		$174,535.22				
* Does not include $1,573,457 of contributions received on June 30, 2009.						

APPENDIX B—VERMONT COMMON TRUST FUND: *Total Return Analysis—Year Ended June 30, 2009*

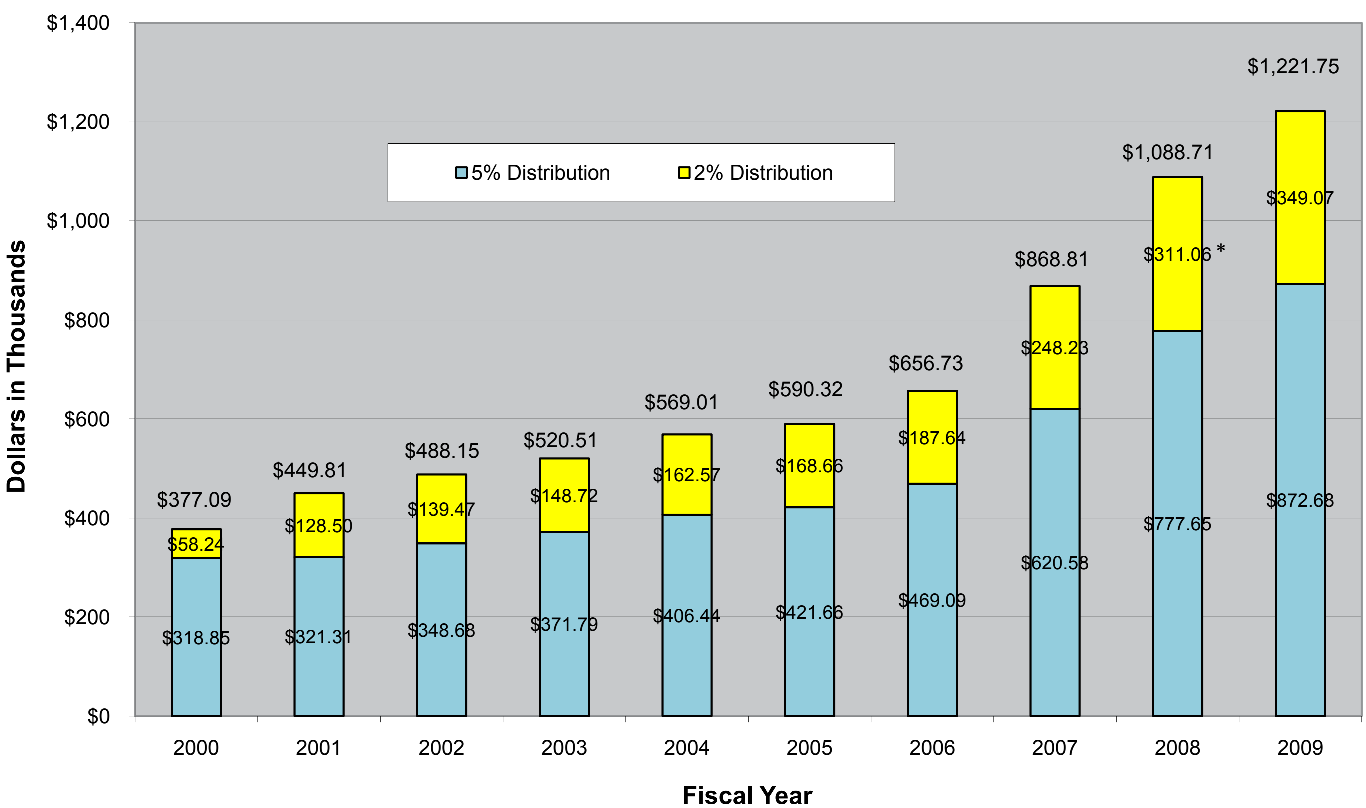
MANAGER	Fiscal Year 2001	Calendar Year 2001	Fiscal Year 2002	Calendar Year 2002	Fiscal Year 2003	Calendar Year 2003	Fiscal Year 2004	Calendar Year 2004	Fiscal Year 2005	Calendar Year 2005	Fiscal Year 2006	Calendar Year 2006	Fiscal Year 2007	Calendar Year 2007	Fiscal Year 2008
DOMESTIC EQUITY															
Hanson Investment Management	29.41%	17.41%	-7.78%	-18.01%	-1.89%	42.55%	29.10%	15.92%	22.25%	19.18%	21.10%	20.28%	29.13%	14.32%	-14.64%
Prentiss Smith & Co.	7.59%	13.69%	3.60%	-7.35%	7.70%	18.17%	11.47%	13.25%	11.00%	10.68%	15.77%	16.61%	20.09%	10.85%	-4.96%
S&P 500	*-13.56%*	*-11.89%*	*-17.99%*	*-22.11%*	*0.25%*	*28.69%*	*19.14%*	*10.90%*	*6.32%*	*4.91%*	*8.63%*	*15.80%*	*20.60%*	*5.50%*	*-13.13%*
DOMESTIC FIXED INCOME															
NL Capital Management	10.34%	10.07%	9.41%	9.48%	8.92%	5.43%	3.48%	5.56%	7.42%	3.07%	0.26%	5.31%	6.12%	7.61%	9.10%
Access Capital*														2.83%	3.52%
Barclays (formerly Lehman) Aggregate	*10.23%*	*8.44%*	*8.63%*	*10.25%*	*10.40%*	*4.10%*	*0.32%*	*4.34%*	*6.80%*	*2.43%*	*-0.81%*	4.33%	*6.12%*	*6.96%*	*7.12%*
TOTAL FUND DOLLAR WEIGHTED RETURN	11.27%	11.62%	7.94%	5.15%	8.59%	11.24%	7.59%	8.14%	10.17%	6.64%	5.86%	9.48%	12.02%	9.47%	3.10%
Total Fund Target	7.52%	6.57%	3.94%	3.29%	9.23%	9.94%	4.96%	6.23%	6.76%	3.27%	2.19%	7.96%	10.62%	6.80%	1.14%
TOTAL FUND MARKET VALUE ($mil.)	$26.5	$32.6	$33.3	$34.9	$37.3	$38.8	$39.3	$41.1	$43.5	$48.6	$49.7	$52.8	$55.5	$58.8	$59.3
* Common Trust Fund Investment Inception date in Access Capital: 10/12/07															

MANAGER	Quarter Ended 9/30/2008	Quarter Ended 12/31/2008	**Calendar Year 2008**	Quarter Ended 3/31/2009	Quarter Ended 6/30/2009	**Fiscal Year 2009**	Portfolio Value 6/30/2009	Portfolio Percent 6/30/2009
DOMESTIC EQUITY								
Hanson Investment Management	-10.64%	-21.33%	**-38.44%**	-8.37%	11.71%	**-28.04%**	$8,759,816	14.8%
Prentiss Smith & Co.	-6.34%	-13.52%	**-23.98%**	-3.74%	16.28%	**-9.34%**	$9,370,912	15.8%
S&P 500	*-8.37%*	*-21.94%*	***-37.00%***	*-11.01%*	*15.93%*	***-26.21%***		*30.6%*
DOMESTIC FIXED INCOME								
NL Capital Management	1.77%	3.34%	**7.81%**	2.43%	0.97%	**8.77%**	$38,288,140	64.7%
Access Capital*	1.61%	1.39%	**3.71%**	3.56%	1.90%	**8.72%**	$2,781,428	4.7%
Barclays (formerly Lehman) Aggregate	*-0.49%*	*4.58%*	***5.24%***	*0.12%*	*1.79%*	***6.06%***		69.4%
TOTAL FUND DOLLAR WEIGHTED RETURN	-1.04%	-1.69%	**-3.62%**	0.39%	4.85%	**2.40%**		
Total Fund Target	-2.55%	-1.68%	**-6.59%**	-2.63%	5.93%	**-1.19%**		
TOTAL FUND MARKET VALUE ($mil.)	**$57.2**	**$55.7**	**$55.7**	**$56.2**	**$59.2**	**$59.2**	**$59,200,297**	**100.0%**
* Common Trust Fund Investment Inception date in Access Capital: 10/12/07								

HIGHER EDUCATION TRUST FUND: *Fund Contributions—Fiscal Years*

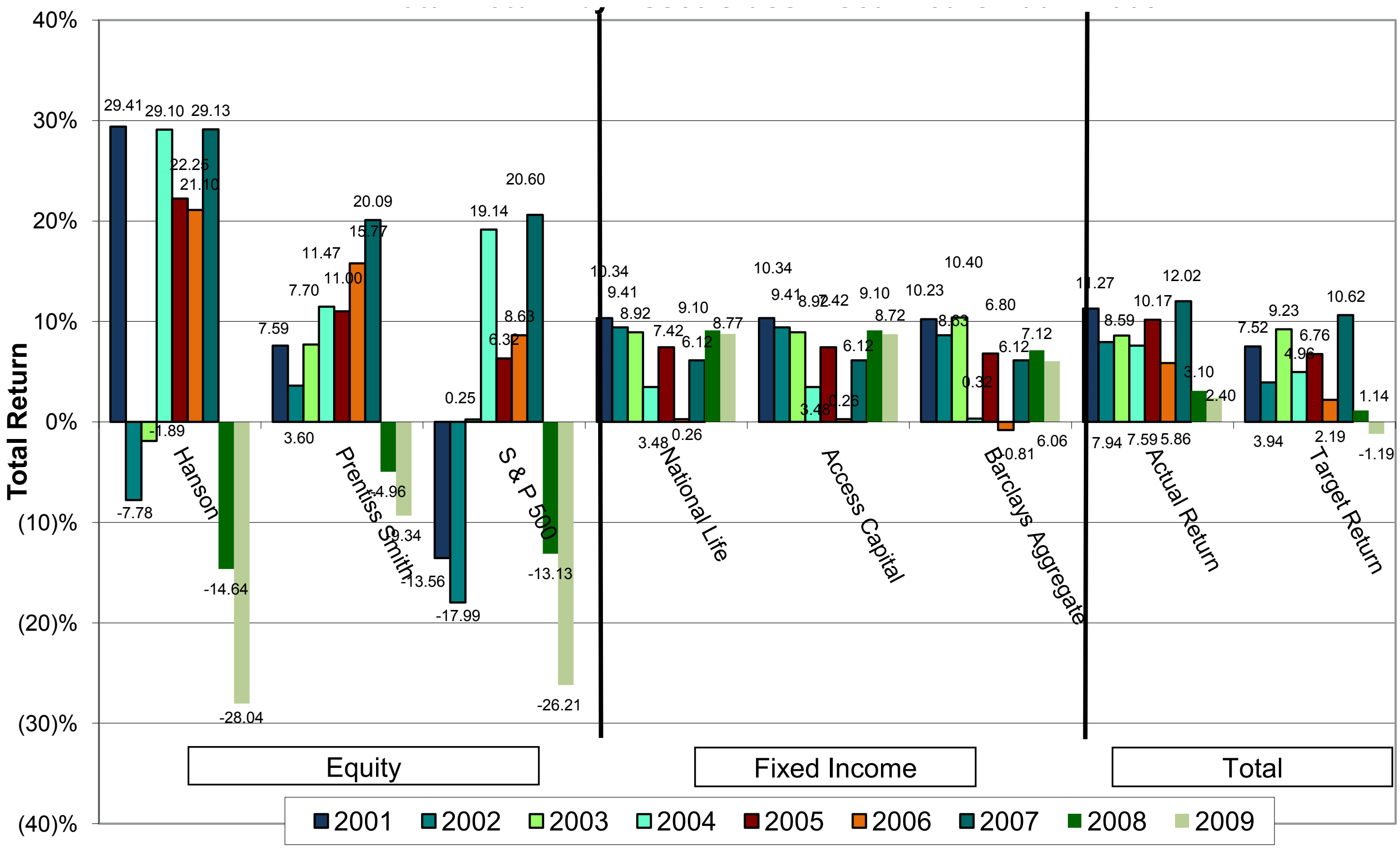


HIGHER EDUCATION TRUST FUND: *Authorized Distributions by Year and Type*

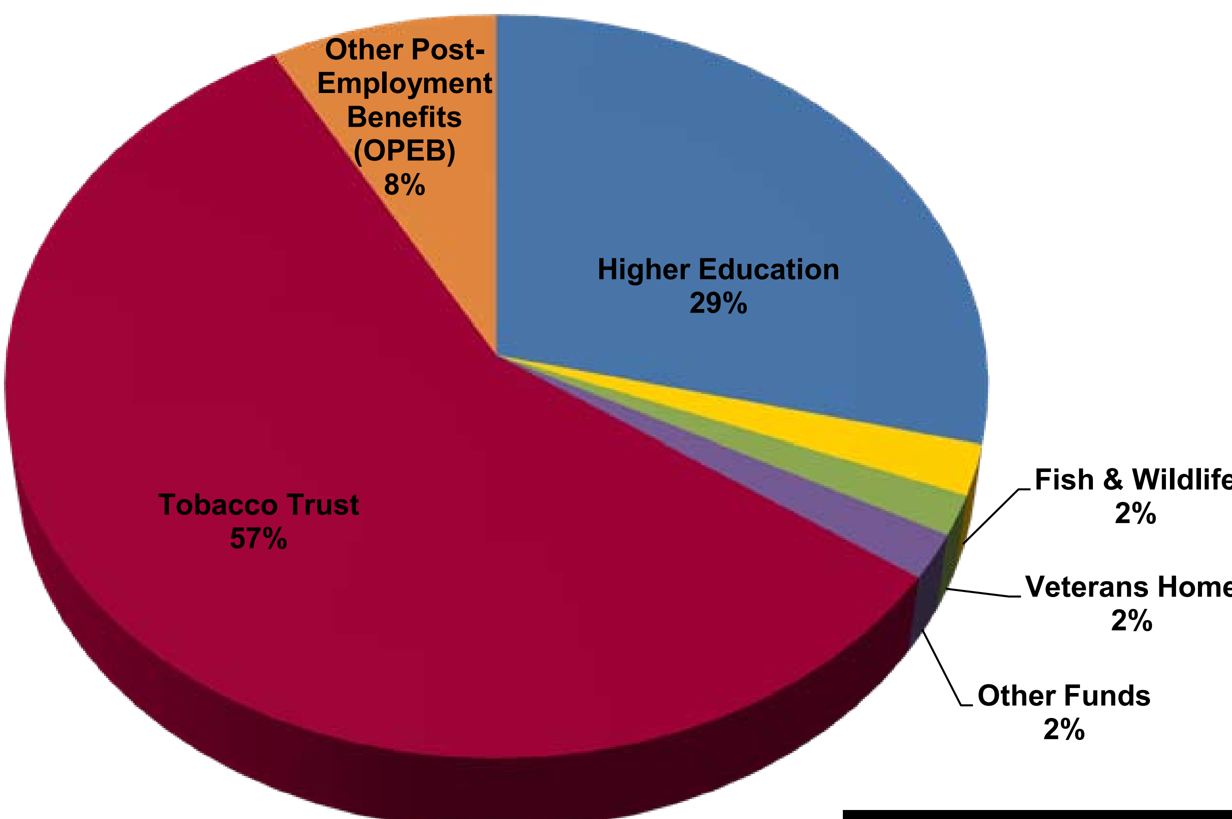


* Actual 2% distribution for 2008 was $298,227.18.

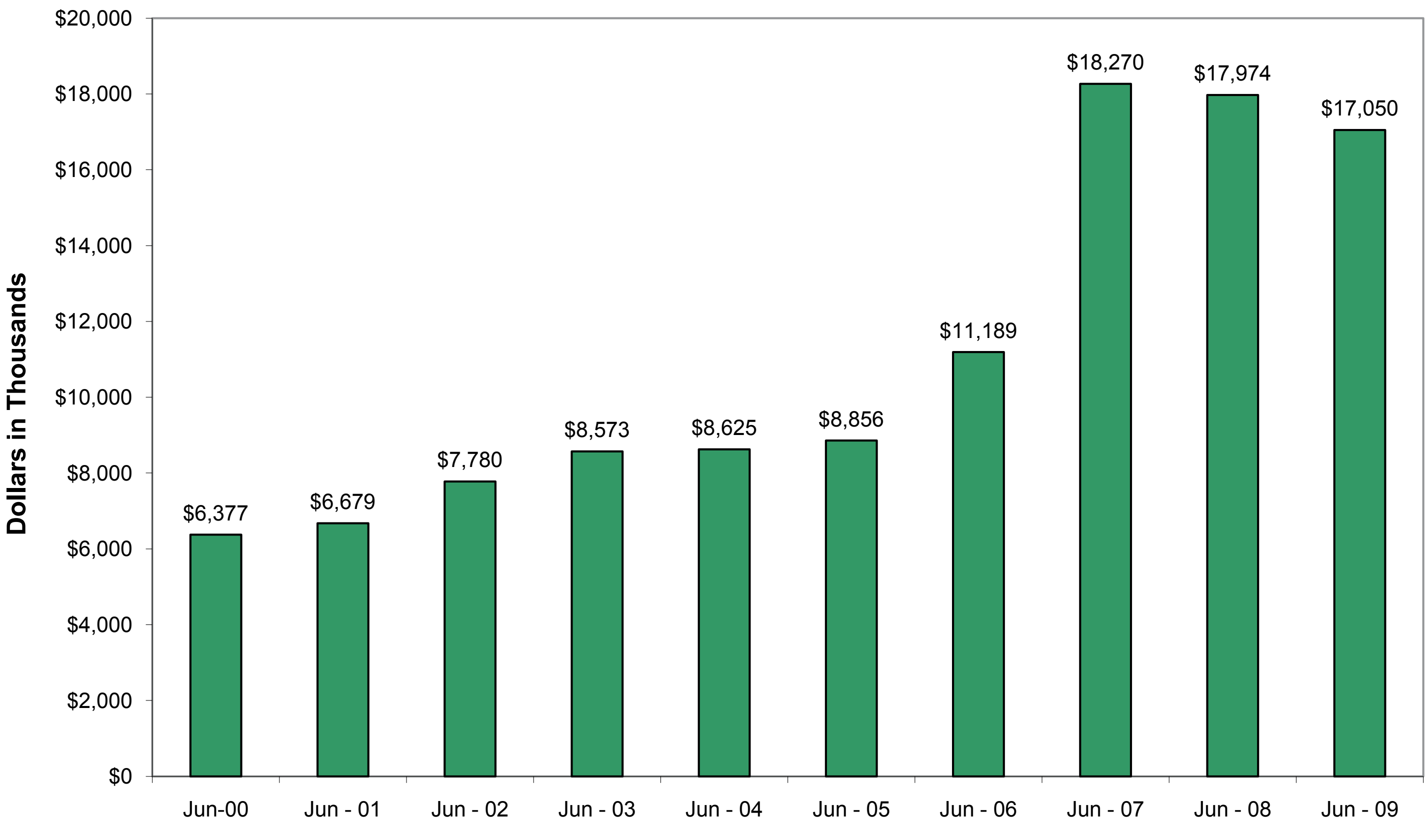
HIGHER EDUCATION TRUST FUND: *Total Return by Asset Class Fiscal Years 2001-2009*



HIGHER EDUCATION TRUST FUND: *Common Trust Fund Breakdown as of June 30, 2009*



HIGHER EDUCATION TRUST FUND: *Asset Growth—6/30/00 to 6/30/09, includes distributions*



OTHER POST-EMPLOYMENT BENEFITS FUNDING ANALYSIS—VSERS & VSTRS

VSERS -- Other Post-Employment Benefits Funding Analysis

	PRE-FUNDING BASIS	PARTIAL FUNDING
Assumed Discount Rate	8.25%	4.25%
Actuarial Value of Assets	$5,748,582	$5,748,582
Actuarial Accrued Liability		
- Active Participants	$234,565,363	$468,333,368
- Retired Participants	219,645,689	312,414,941
- TOTAL	$454,211,052	$780,748,309
Unfunded Actuarial Liability	$448,462,470	$774,999,727
Funded Ratio	1.3%	0.7%
Annual Covered Payroll	$426,826,921	$426,826,921
Unfunded Actuarial Liability (as % of covered payroll)	105.1%	181.6%
Normal Cost for FY 2009	$15,091,245	$34,759,864
Amortization of Unfunded Actuarial Liability (for FY 2010 -30 yr)	$22,467,374	$23,238,214
Annual Required Contribution (ARC) FY 2010 *	$37,558,619	$57,998,078
Expected Benefit Payments	$25,191,706	$25,191,706
Increase in Annual Cost to Fund Plan	$12,366,913	N/A

** Payment is assumed to be made at the beginning of the fiscal year.*

VSTRS -- Other Post-Employment Benefits Funding Analysis

	PRE-FUNDING BASIS	PAY-AS-YOU-GO BASIS
Assumed Investment Return	8.25%	4.00%
Actuarial Value of Assets	$0	$0
Actuarial Accrued Liability		
- Active Participants	$192,870,008	$480,458,989
- Retired Participants	239,017,971	391,777,332
- TOTAL	$431,887,979	$872,236,321
Unfunded Actuarial Liability	$431,887,979	$872,236,321
Funded Ratio	0%	0%
Annual Covered Payroll	$561,588,013	$561,588,013
Unfunded Actuarial Liability (as % of covered payroll)	76.9%	155.3%
Normal Cost for FY 2009	$10,559,025	$33,745,199
Amortization of Unfunded Actuarial Liability (for FY 2010-30 yr)	$21,637,014	$25,221,028
Annual Required Contribution (ARC) FY 2010 *	$32,196,039	$58,966,227
Expected Benefit Payments	$17,960,564	$17,960,564
Increase in Annual Cost to Fund Plan	$14,235,475	N/A

** Payment is assumed to be made at the beginning of the fiscal year.*

Report of the Commission on the Design and Funding of Retirement and Retiree Health Benefits Plans for State Employees and Teachers

Recommendations to the Governor and the General Assembly

December 2009

Guiding Principles for a Retirement Plan

Fairness and Sustainability Are Both Essential to Benefit Plans

What Do We Want From Our Retirement Benefit Plan?

- **Recruitment – The benefit plan should act as an incentive for recruiting high quality employees. The plan must be competitive with those in other states and within Vermont.**
- **Retention – The benefit plan should act as an incentive for retaining high-quality employees and maintaining a stable workforce. The plan should also be compatible with changing workforce and demographic trends**.
- **Reward – The benefit plan should provide a solid foundation for retirement security following a career in public service.**
- **Sustainability – The cost of the benefit plan should be sustainable and predictable over the long term**.
- **Affordability – The cost of the benefit plan should be affordable for current and future public employees and other taxpayers**.
- **Fairness – The benefit plan should be fair to workers and other taxpayers.**
- **Equity – The benefit plan should be equitable for all parties.**

"A broad deterioration in funding levels for public sector pensions is adding to fiscal pressure on some state and local governments and could contribute to negative rating actions for select issuers in the next several years."

- ***Moody's investors Service, November 2009***

"Even if financial markets improve, and help retirement trust funds recover, the state fiscal crisis, political, and demographic issues will continue their stress on retirement systems."

- ***NCSL Fiscal Leaders Seminar, December 2009***

"The driving force behind the growing cost of retirement is the fact that the baby boomers will spend more time in retirement than any previous generation. According to the Center for Disease Control, a 65-year-old can now expect to live another 18 years, on average. American seniors are living 50 percent longer than they were in the 1930s, when Social Security set 65 as the benchmark retirement age"

- ***PBS Frontline Report, May 2006***

Executive Summary

The 2009 General Assembly created the Commission on the Design and Funding of Retirement and Retiree Health Benefits Plans for State employees and Teachers to review and report on the design and funding of retirement and retiree health benefit plans for the State employees' and teachers' retirement systems. The Joint Fiscal Committee provided the Commission with a target for the expenditure growth rate of 3.5 percent. Similar efforts are occurring across the country because the costs of maintaining retirement programs have been increasing faster than states' ability to pay for them.

The Legislature, Governor, employees, and taxpayers are all concerned about the affordability and long-term sustainability of the pension and retiree health care plans. Certainly, the serious implosion of the financial markets in 2008 and the first quarter of 2009 is the largest factor in the very large increase in this year's actuarially required contribution, but demographics, workplace trends, and current benefit provisions also play an important role and are adding significant stress on the State's ability to maintain adequate pension plan funding. There are 2,800 more retired teachers and State employees this year than there were in 2003. Pension benefit payouts for State employees and teachers have been increasing by roughly $10-11 million each year in recent years and are now increasing by $15-16 million each and every year. It is not uncommon to have employees begin drawing their pension and retiree health benefits in their early to mid-fifties. With increasing life expectancies, these people may well receive retirement benefits for more years than they had spent in employment with the State or the school districts.

The State's combined actuarially required contribution this year is $73.5 million and, without changes being implemented, will be $103.5 million next year. That is a $32-million one-year increase in a year when the State is facing a budget deficit recently estimated in the $150 million range. Simply put, financial commitments for pension and health benefit programs are growing much faster than the rate of revenue growth or the ability of taxpayers to pay for them.

The Commission looked at ways to address this within the context of a set of guiding principles for our retirement plans, including recruitment and retention of high quality employees, provision of a solid foundation for retirement security, fairness, affordability, and sustainability. The recommendations adopted by the Commission and included in this report are intended to address those considerations. We also recognize that these pension benefits are a significant contributor to Vermont's economic health. When retirees spend their pension benefits to buy products, they create demand for goods and services, resulting in jobs. A recent report by the National Institute on Retirement Security estimated that retiree expenditures stemming from state and local pension benefits supported close to 1,400 jobs in Vermont. The report stated that retirement benefits also have a large multiplier effect, creating additional economic activity. As retirees pay income tax on their benefits, this is an important revenue source for the operation of government. However, these positive economic contributions cannot be maintained if pension benefit cost increases exceed the ability of taxpayers to afford them.

The recommendations made in this report, if adopted, would cut the FY 2011 actuarially required contributions for the State pension system from the actuary's recommendation of $41.6 million to $33.1 million and for the teachers' pension system from $63.5 million to $43.0 million, a combined reduction of $29 million or 28 percent, and would produce significant savings for many years. This also meets the Joint Fiscal Committee's 3.5 percent benchmark. Of the $29 million reduction in the State's FY 2011 contribution, $12 million results from benefit revisions and $17 million comes from increased employee contributions. We have also proposed recommendations to adjust the premium assistance for health coverage for future retirees, recognizing at the same time the need for the State to begin a plan for funding these important future liabilities.

Later in this report we will address what groups of active State and teacher employees would be affected by the various recommendations. *Under no circumstances, however, do we consider any recommendations of this report to apply to current retirees of either system.* These individuals have ended their public service careers with an agreed-upon income benefit.

The recommendations of this Commission, therefore, attempt to strike a balance, recognizing the public policy and economic context in which the current benefit structures operate. We do not make these recommendations lightly and hope that the Legislature and the Governor recognize the urgent need to balance these concerns and create sustainable plans. Change will occur, either by careful long-term planning or by default. We are fast approaching the tipping point where the failure to address the issue now will lead to potentially larger problems later and the need for more draconian steps, failing both the employees and the taxpayers.

While we believe that these recommendations provide a solid course of action, we also recognize that there is a range of options inherent in each, with varying impacts on the overall cost of benefits. We see this report as the foundation of a meaningful dialogue within which varying features can be reviewed and adjusted. The Commission looks forward to working with all interested parties through the coming legislative cycle to meet our mutual goal of a fair, equitable, and sustainable retirement system that provides benefits to the labor force and the state economy.

Key Findings

General

- Funding for retirement benefits, including health care, is among the largest fiscal challenges facing many state governments, including Vermont. Financial commitments for these programs, especially retiree health insurance, are growing much faster than the rate of revenue growth.

- While some of the State's pension costs are paid for through other than the General Fund, a comparison of the required annual contributions to the total General Fund revenues indicates an alarming trend. The State's combined actuarial pension contribution in fiscal year 2008 ($66.3 million) represented about 5 percent of General Fund revenues ($1.2 billion). The State's combined actuarial pension contribution this year ($71.5 million) represents about 7 percent of the General Fund revenues ($1.0 billion). The State's projected actuarial contribution for fiscal year 2011, assuming no changes, represents about 9.5 percent of the expected General Fund revenues ($1.1 billion). When health care liabilities are added to the total, it is clear that these programs put excessive budgetary pressure on available revenues and are crowding out other important State expenditure items.

- The Joint Fiscal Committee considered the recent performance of a number of indicators that reflect State revenue and spending trends and broader economic trends, including the general fund growth rate and the state and local price index. After considering this information, the Joint Fiscal Committee recommended to the Commission a target of 3.5 percent for the rate of expenditure growth for retirement and health benefits. The current pension fund growth, not including any unfunded liabilities or investment loss, assumes a growth rate of approximately 4.5 percent. Amortization schedules increase at 5 percent. For health, actuarial assumptions vary by year, but all exceed the benchmark. Since no significant prefunding has occurred for VSERS and none at all for VSTRS, significant funding in the order of $47.8 million would be needed just to bring current the annual actuarially required contribution (ARC) for each system, on a prefunded basis. Costs escalate even further without prefunding.

- Investment upturn will not get the state out of this problem. Our actuaries estimate <u>that it will take more than 20 years</u> at our current actuarial investment rate of return of 8.25 percent to get back to fiscal year 2008 funding level. It should be noted that the current assumed rate of return is on the high side when compared to other plans, with close to 75 percent of other plans using a return assumption less than 8.25 percent. Also, keep in mind that the FY 2008 levels were not fully funded (94.1 percent for VSERS and 80.9 percent for VSTRS). It would not be prudent to rely on future market returns above the assumed rate of return to solve the problem.

Pension Benefits

- As noted, the State's combined actuarially required contribution this year is $73.5 million and, absent changes being implemented, will be $105.1 million next year, almost a $32 million one-year increase:

Pension Funding Requirements:	STATE EMPLOYEES	TEACHERS
FY 2010 Annual Actuarial Required Contributions (ARC):	$32 million	$41.5 million
FY 2011Annual Actuarial Required Contributions (ARC):	$41.6 million	$63.5 million
Additional Resources Needed to Fund FY11 Estimated ARC over FY10 Levels:	<u>$9.6 million</u>	<u>$22 million</u>
TOTAL ADDITIONAL RESOURCES NEEDED FOR *BOTH* SYSTEMS:	**$31.6 million**	

- The ARC has been increasing at an unsustainable pace, even before consideration of current economic events. Prior to the market meltdown, the annual actuarially recommended contribution (ARC) (pension only, excluding expenses) for the State system increased 117 percent over a five-year period from FY 2003 to FY 2008. The current ARC recommendation by the actuary, absent any recommendations included in this report, is $41,581,656 for FY 2011 and represents a 328 percent increase compared to FY 2003, even after re-amortization implemented in FY 2010.

- For the teachers' system, the ARC increase from 2003 to 2008 was 46 percent, reduced by re-amortization of the unfunded liability in FY 2007. The ARC increased just over 100 percent from FY 2003 to FY 2006, prior to re-amortization. The current ARC recommendation, absent any recommendations included in this report, will rise to $63,501,209, a 53 percent increase in one year.

- As of the FY 2008 valuation, the State pension system (VSERS) had an unfunded liability of $87.1 million while the Teachers' system had an unfunded liability of $379.5 million. The FY 2009 unfunded liabilities have increased to $326.5 and $727.8 million, respectively, significantly reducing the funding ratio.

Pension Liabilities

UAAL (pension only)	**STATE EMPLOYEES**	**TEACHERS**
As of 6/30/08 Valuation:	$87.1 million	$379.5 million
As of 6/30/09 Valuation:	$326.5 million	$727.8 million
Funding Ratio		
As of 6/30/08 Valuation:	94.1 percent	80.9 percent
As of 6/30/09 Valuation:	78.9 percent	65.4 percent

- There are 2,800 more retired teachers and State employees this year than there were in 2003.

- Due to the aging of the workforce and current retirement age provisions, the rate of growth in retirees has been outpacing the rate of growth in active members. This creates additional stresses, especially given current levels of underfunding, and could impact pension asset allocation in the future as more liquid assets are needed to pay benefits.

- Pension benefit payouts for State employees and teachers have been increasing by roughly $10-11 million each year in recent years and are now increasing by $15-16 million each and every year.

- Five years ago the annual benefit payouts for State employees and teachers totaled $111.6 million; this year the annual payout is projected to be $172 million, and in five years an independent actuary projects the annual benefit payout will be $255.8 million. That will be close to a 50 percent increase from what the annual benefit payout is now.

Health Care Benefits

- Beginning in FY 2008 the Government Accounting Standards Board required the disclosure of other post employment benefits (OPEB) in the State's financial reports. OPEB refers to any post employment benefit other than pensions, although medical is the most significant component.

- Currently the State does not prefund its OPEB benefits, with the exception of a small portion of Medicare D reimbursements from the State Employees' system. The State system is 0.7 percent funded; while the teachers' system is 0 percent. In other words, little or no assets have been set aside for this liability.

- OPEB liabilities are as follows:

Vermont OPEB Liabilities

STATE EMPLOYEES	**8.25% (Pre-funding Assumed)**	**4.25% (Partial Funding Basis)**
Unfunded Liability:	$448.5 million	$775 million
ARC for FY 2010:	$37.6 million	$58 million
Pay-As-You-Go Applied to ARC:	$22 million	$22 million
TEACHERS		
Unfunded Liability:	$431.8 million	$872.2 million
ARC for FY 2010:	$32.2 million	$59 million

- Payments for the 80 percent employer share for retiree health insurance premiums are projected to escalate by several million dollars a year.

	VSTRS Retiree Health Payment	**VSERS Retiree Health Payment**
FY 2008	$15.08 million	$16.37 million
FY 2009	$16.42 million	$17.89 million
FY 2010	$18 million estimated	$22 million estimated

- By 2020 the actuary estimates health care pay-as-you-go payments for teachers will more than double, at $38.3 million, and will reach $77.4 million by 2040. For the State system, the pay-as-you-go payments will reach $46.5 million in 2020 and $73.8 million by 2040.

- ➢ The State currently funds a year's premiums in the State Employees' system; expenses are not explicitly funded in the teachers' system, creating further actuarial losses in the pension system from which benefits are paid. Since health care for teachers is paid by the pension fund, IRS limitations will soon force curtailment of benefits if mitigating steps are not taken.

Key Recommendations

The Commission, by a majority vote, recommends the following: (For details, see Commission Votes section of this report.)

CATEGORY: General Framework

RECOMMENDATION ONE

Make **no change** to the following:

- Pension or retiree health benefits for those already retired.
- Pension or retiree health benefits for anyone close to retirement, which the Commission defined as within five years of eligibility for a particular benefit.
- Basic provisions (maximum benefit, multiplier, COLA, etc.) that would make the plans less competitive than the mainstream of other state public systems.

RECOMMENDATION TWO

Do not replace the current defined benefit plan and transition to a defined contribution plan.

RECOMMENDATION THREE

That the Legislature and the Governor continue to fully fund the annual actuarially required contribution (ARC) for the state and teachers' pensions, as calculated after any or all recommendations made below are enacted. Continued discipline in fully funding the ARC is critical to the long-term sustainability of the pension funds.

RECOMMENDATION FOUR

That the Legislature, without delay, develop and implement a structural plan to fund OPEB obligations and set money aside in a material way through a separate, independent funding mechanism.

In addition, the Commission voted not to take a position on shifting the State's payment for the teacher's retirement plan from the General Fund to the Education Fund or local districts.

CATEGORY: Pension Plan Recommendations

RECOMMENDATION FIVE

Revisions to normal and early retirement ages:
State Group F and Teachers' Group C:

- Raise normal retirement age from 62 or 30 years at any age to 65 or rule of 90 (combination of age and years of service) for those more than five years from normal retirement eligibility.

  It should be noted that "five years from normal retirement eligibility" for purposes of these recommendations means the member must be either 5 years or less from normal retirement age for their group plan, or have a minimum of 25 years of service as of the date the retirement legislation is enacted. If a member has begun making a purchase of service that is documented in the system prior to December 31, 2009, the total years of service being purchased may count toward the total years of service as of the effective date of the legislation. No service that is initiated after January 1, 2010 will count toward total creditable service as of the effective date.

  Raise the early retirement age from 55 to 58 for those more than five years from early retirement eligibility. Change the early retirement penalty to full actuarial reduction.

State Group D:

- Raise normal retirement age from age 62 to age 65 for those more than five years from normal retirement eligibility.

State group C:

- Raise the early retirement age to 52 from 50 for those more than five years from early retirement eligibility.

RECOMMENDATION SIX

Lengthening the salary compensation period:
State Group F and Teachers' Group C:

- Use a five-year compensation period instead of a three-year period to calculate benefits for those more than five years from retirement eligibility.

State Group C:

- Use a three-year compensation period instead of a two-year period to calculate benefits for those more than five years from retirement eligibility.

State Group D:

- Use a two-year compensation period instead of final salary to calculate benefits for those more than five years from retirement eligibility.

RECOMMENDATION SEVEN

Increase the maximum benefit from 50 percent to 60 percent of final compensation for State Group F and Teachers' Group C for those more than five years from retirement eligibility.

- This would provide an opportunity for increased benefits to employees who choose to work more than 30 years. Right now most teachers and State employees are capped at their maximum retirement benefit of 50 percent of average final compensation after 30 years of service. With this change, one would receive 60 percent of AFC after 36 years of service.

RECOMMENDATION EIGHT

Revising the contribution rate ratio and rates for employer and employees:

While contribution levels for State employees and teachers have remained constant in recent years, the State's employer share, as a percentage of payroll, is expected to continue escalating. Instead of having a fixed employee contribution rate set in statute, with the State/employer contribution rate floating on an annual basis, the Commission recommends a proportional contribution system between the State and employees/teachers. The Commission chose to recommend a sharing of the total annual contribution, with the State share capped at the 3.5 percent to accommodate the growth target set by the Joint Fiscal Committee. The result, assuming all other recommendations are enacted, is as stated below and compared to the baseline if no recommendations are enacted. A similar rate increase would occur in the other group plans.

Recommended Rate/Risk Sharing Impact

	Employer ARC	Employee Contribution %	State Contribution %
VSERS			
FY 2011 actuarial recommendation, no changes	$41.6 Million	5.10% (Group F)	9.80%
FY 2011 recommendation, changes, 3.5% state increase	$33.1 Million	5.83%	7.84%
VSTRS			
FY 2011 actuarial recommendation, no changes	$63.5 Million	3.40% (Group C)	9.67%
FY 2011 recommendation, changes, 3.5% state increase	$43.0 Million	5.47%	7.32%

Employee contributions in both systems are pre-tax contributions under Section 414(h) employer pick-up provisions and will therefore reduce the member's tax liability while he or she is employed. In contrast, Social Security and Medicare taxes are not considered pre-tax deductions, and therefore are included in the total taxable income when calculating federal and state taxes each pay period. Later in this report, there is a full chart with a number of other rate-sharing models reviewed by the Commission. It is important to remember that rate/risk sharing creates a partnership; employer and employee contributions will rise and fall in tandem. Both parties will have a stake in keeping benefit, administrative, and other costs in check. If investment returns perform very well for an extended period, both parties will enjoy a decrease in contribution levels. The new contribution rates would apply to all State employees and teachers.

CATEGORY: Health Care Recommendations

RECOMMENDATION NINE

The Commission recommends a tiered medical premium co-payment structure based on length of service. Instead of the current straight 80/20 split of retiree health insurance premiums utilized for most retired teachers and State employees (new hires in the State system after July 1, 2008, have a tiered system), a new tiered system would apply to all of those not within five years of eligibility to draw this benefit. In recognition of the fact that the Group C plan of the State employees retirement system is essentially a 20 year plan, the Commission recommends a pro-rated tiered medical premium co-payment for Group C plan members.

The new employer share for the tiered system would be:

40 percent - 10 yrs 60 percent - 20 yrs 80 percent - 30 yrs

Note: Retirees with less than 10 years would have access to group health insurance, but would have to pay the full premium.

RECOMMENDATION TEN

The Commission recommends providing the ability to "recapture" the retiree health benefit to those vested, terminated members with 20 or more years of service when they begin drawing benefits. This opportunity is not currently allowed for general State employees and is allowed for teachers with 10 or more years of service.

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