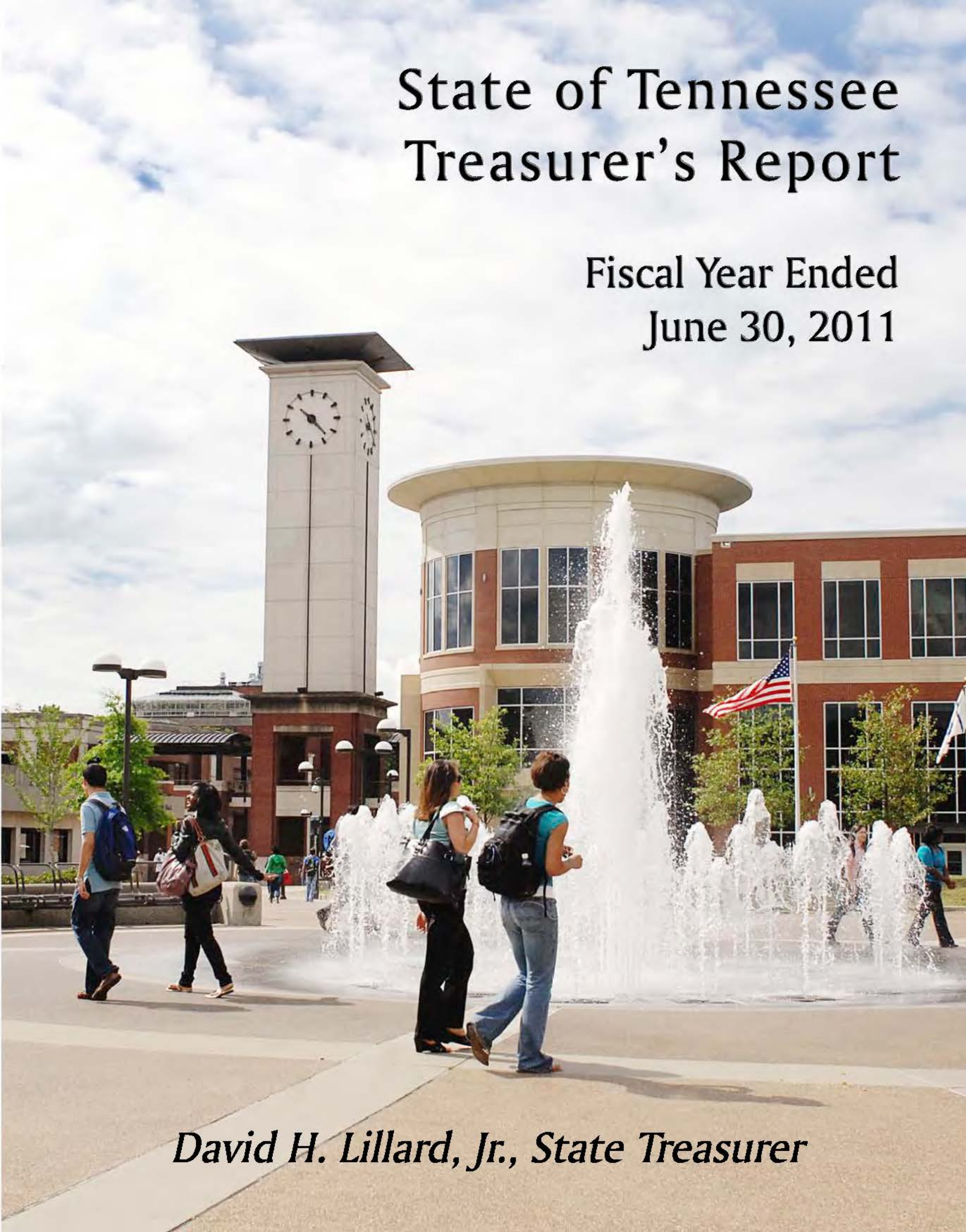
# State of Tennessee Treasurer's Report

## Fiscal Year Ended June 30, 2011



*David H. Lillard, Jr., State Treasurer*

# 2011
# Treasurer's Report

**David H. Lillard, Jr., Treasurer**
**State of Tennessee**

**Prepared by:**

**State of Tennessee**
**Treasury Department**
**1st Floor State Capitol**
**Nashville, Tennessee 37243**
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The photographs featured within this report
spotlight main attractions located in
Memphis, Tennessee;
hometown of our State Treasurer,
David H. Lillard, Jr.

The cover features the University of Memphis.

*The University of Memphis was founded under the auspices of the General Education Bill, enacted by the Tennessee Legislature in 1909. Originally known as West Tennessee State Normal School, the institution opened its doors September 10, 1912.*

*Students in the first classes selected blue and gray as the school colors and the tiger as the mascot. Tradition holds that the colors, those of the opposing armies during the Civil War, were chosen in commemoration of the reuniting of the country after that divisive conflict.*

*In 1925, the name of the college changed to West Tennessee State Teachers College. The college changed names again in 1941, becoming Memphis State College.*

*In 1957, the state legislature designated Memphis State full university status. In 1959, the university admitted its first black students and the first doctoral programs began in 1966.*

*Today, the University of Memphis is one of Tennessee's three comprehensive doctoral-extensive institutions of higher learning. Situated in a beautiful park-like setting in the state's largest city, it is the flagship of the Tennessee Board of Regents System. It awards more than 3,000 degrees annually.*

*With an enrollment of approximately 21,000 students, the University of Memphis has 24 Chairs of Excellence, more than any other Tennessee university, and five state-approved Centers of Excellence.*

Photographs compliments of:
Andrea Zucker
Baxter Buck
Kevin Barre Photography
Memphis Convention and Visitors' Bureau
Mud Island River Park
National Civil Rights Museum
Tennessee's Department of Tourist Development
Tennessee's Photographic Services
University of Memphis

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**This report is available in its entirety on the Internet at:**
**http://treasury.tn.gov/TreasurersAnnualReport_2011.pdf**



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# LETTER OF TRANSMITTAL

STATE OF TENNESSEE

**TREASURY DEPARTMENT**
STATE CAPITOL
NASHVILLE, TENNESSEE 37243-0225

February 15, 2012

The Honorable Bill Haslam, Governor
The Honorable Ron Ramsey, Speaker of the Senate
The Honorable Beth Harwell, Speaker of the House of Representatives
Members of the General Assembly
Citizens of the State of Tennessee

Ladies and Gentlemen:

It is my honor to present the annual report of the Treasurer's office for the fiscal year ended June 30, 2011, pursuant to the requirements of Section 4-4-114, Tennessee Code Annotated.

With your continued support and the outstanding employees in the Treasury Department, we have made tremendous advancements and continue to enhance our existing capability to better serve the citizens of Tennessee. This year was a busy year for our department as we began work to implement the Concord Project. Concord is a new computer system that will provide more efficient Tennessee Consolidated Retirement services for employers, active employees and retirees. As we continue on the path of implementation for this project, we will communicate our progress to you.

The Treasury Department completed a non-traditional project for the department – a *History of State Treasurers* project. My staff researched and contacted descendents of former treasurers to document information on state treasurers since the inception of the office. This information is available on the Treasury website and is included in this year's publication of the Tennessee Blue Book published by the Tennessee Secretary of State's office.

For your convenience, the Treasurer's Report, other publications and press are located on our website at www.tn.gov/treasury. Again, thank you for your service to the state of Tennessee and her People.

Sincerely,

David H. Lillard, Jr.
Tennessee State Treasurer

# MISSION OF THE TREASURY DEPARTMENT

## *Vision Statement*

To be faithful stewards of the state's financial and human resources. To be passionate about achieving our mission and living by our core values.

## *Mission Statement*

We will be a leader by providing exceptional service to our customers honestly, efficiently, and effectively.

## *Treasury Team Commitment*

In order for us to provide exceptional service, both management and employees will foster an environment that respects, challenges, motivates, and rewards each team member. Each of us has a responsibility to develop and maintain this environment so that, together, we can achieve our mission and live by our core values.

## *Department Core Values*

*Impeccable Honesty*: We will develop relationships and interact with one another and with our customers in a manner that fosters and encourages trust. We will maintain the highest ethical and professional standards in everything that we do.

*Mutual Respect*: We will treat everyone equitably and with honor. We will communicate in a manner that promotes open dialogue with our customers, within the department, and with our peers in state government.

*Continuous Improvement*: We will continually challenge ourselves to improve the level of service that we provide by being innovative, collaborative, creative, and efficient. We will work to be the best at what we do.

*Shared Accountability*: We will work as a team and will purposely strive to leverage the strengths and overcome the weaknesses of each team member. We will accept responsibility individually and collectively for the service that we provide to our customers.

*Exceptional Service*: We will be innovative in how we provide services to our customers and in how we do our work. We will be relentless in our pursuit of quality and excellence in everything that we do. We will focus not only on solving customers' problems, but also anticipating their needs.

*Exemplary Leadership*: We will be visionary leaders and positive role models for our peers. We strive to be highly respected both inside and outside state government.

# EXECUTIVE SUMMARY

## Introduction

The 2011 Treasurer's Report contains reports on various programs administered by the Treasury Department. The following comments represent a brief statement of the purpose and operations of programs administered by the department. The remainder of this report gives detailed data regarding the activities of these programs during the 2011 fiscal year.

## Baccalaureate Education System Trust (BEST)

The Baccalaureate Education System Trust (BEST) is a Section 529 qualified tuition program that allows anyone to save for higher education costs on behalf of a beneficiary. One such plan is a 529 College Savings Plan. Currently, Tennessee does not have an active 529 College Savings Plan, but the Treasuer's Office expects to launch a new college savings plan in the first half of calendar year 2012. The other type of 529 College Savings Plan is the BEST Prepaid Plan (educational services plan) which was introduced in 1997. At June 30, 2011, the BEST Prepaid Plan held 8,830 active contracts with net assets totaling $100.5 million. On November 22, 2010, the BEST Board suspended the ability for participants to make contributions to existing prepaid accounts or to open new prepaid accounts.

## Careers NOW Program

The Careers NOW Program provides Tennessee college students, and students who are residents of Tennessee, but attend an out-of-state college or university, the opportunity to learn more about the operations of the three constitutional offices. It is a paid internship program and interns earn a competitive hourly rate. The program strives to provide students a meaningful work experience and exposure to a professional work environment. This program also broadens the awareness of students and educational institutions relative to the role of the three constitutional offices and the careers available within these offices. Students also have the opportunity to apply textbook theory to real work situations. Since the inception of the program in 1996, over 275 students have participated in the program and approximately 22% of our participants have been hired into full-time positions throughout state government.

## Certified Public Administrator

The University of Tennessee Institute for Public Service administers the "County Official's Certificate Training Program Act." Certain full-time county officers are eligible for an educational incentive payment if the officers have completed the continuing education requirements of the program. Upon certification by the UT Institute for Public Service, the Treasurer's Office pays the incentive payment to certificate holders. In fiscal year ended June 30, 2011, a total of $406,036 was paid by the Treasury to 332 certificate holders.

## Chairs of Excellence

The Chairs of Excellence Trust is a permanent trust fund authorized in 1984 to further the cause of higher education in Tennessee. The funding of the program is provided through contributions made by a private donor and a matching amount by the state, thus, creating a chair. Income from the chair is used to offset the cost of retaining a nationally or regionally recognized scholar at a state college or university who teaches in a specified academic area. Since 1984, a total of 99 chairs have been created. The fair market value of the assets of the 99 chairs totaled $243 million at June 30, 2011. Since the inception of the program, more than $272.5 million of investment income has been generated. More than $148.1 million has been spent by the 99 chairs.

## Claims administration

The Division of Claims Administration is responsible for investigating and making determinations on claims made against the state for workers' compensation by state employees, employee property damage, tort liability and criminal injury compensation. Staff support from the Division of Claims Administration also assists the Board of

# EXECUTIVE SUMMARY

Claims. The Division of Claims Administration received 5,136 claims for tort, employee property damage and workers' compensation. Payments made during the year for workers' compensation, tort and employee property damage claims totaled $31.2 million. The division received 5,905 criminal injury, drunk driver and sexual assault forensic exam claims. Payments made totaled $13.9 million. Since the first payments were issued in 1982, more than $228 million has been paid to crime victims.

## Claims Commission

The Tennessee Claims Commission is an administrative tribunal created to determine monetary claims against the State of Tennessee. There are three commissioners, one from each grand division of the state. At June 30, 2011, the commission had 631 open claims.

## Deferred Compensation Program

The State of Tennessee Deferred Compensation Program offers state employees the opportunity to accumulate supplemental retirement income on a tax-advantaged basis. Participants may direct the investment of their deferred salary into a variety of investment products contracted for the program. During the fiscal year, the state, the University of Tennessee and Board of Regents each matched their employees' contributions to the 401(k) plan at $50 per month. As of June 30, 2011, a total of 80,668 state and higher education employee accounts were held in the program. The market value of accumulated account balances totaled $1.5 billion.

## Flexible Benefits Plan

The State of Tennessee Flexible Benefits Plan is an optional benefit plan which enables state employees to pay for certain expenses with before-tax dollars. At June 30, 2011, state employees utilized the plan in the following manner: 38,546 paid group medical premiums, 27,858 paid group dental premiums, 5,300 used the medical expense reimbursement account and 408 used the dependent care reimbursement account. In addition, 203 and 90 state employees utilized the parking and transportation reimbursement accounts, respectively.

## Investments

The Investment Division has the responsibility for investing all funds under management of the Treasury Department.

State Cash Management - This division manages the State Pooled Investment Fund which includes the state's cash, the various dedicated reserves and trust funds of the state and the Local Government Investment Pool. During 2011, investments averaged $7.1 billion, producing $17.9 million in income for an average rate of return of .26%.

Pension Fund Investments - This division manages the investments of the Tennessee Consolidated Retirement System (TCRS) which, at June 30, 2011, totaled $33.7 billion at fair market value. For the year, investment income of $5.52 billion was recognized, for a rate of return of 19.6% on a fair value basis. The Investment Division also manages investments for the Chairs of Excellence Trust and the Baccalaureate Education System Trust which, at June 30, 2011, had market values of $243.1 million and $100.5 million, respectively.

## Optional Retirement Plan

The Optional Retirement Plan is a defined contribution plan. Investments are participant directed, selected from options offered through the plan service providers using bundled contracts. Contributions to ORP for the year ended June 30, 2011 were $81.2 million and ORP assets were $2.55 billion. There were 11,562 ORP participants at June 30, 2011.

# EXECUTIVE SUMMARY

## Risk Management

The Division of Risk Management is responsible for identifying the state's exposure to property and casualty risks and determining the appropriate risk control methods to protect the state against monetary loss due to unforeseen events. The division administers the state's property and casualty insurance program, including the procurement of all-risk, replacement cost property insurance for all state-owned buildings and contents, builders' risk insurance for new construction, fine arts insurance to protect all types of valuable artwork and items of antiquity, boiler insurance and inspection services for all state-owned boiler objects, fidelity and crime coverage to protect against employee dishonesty and aviation insurance for the state's aircraft. The state procures its insurance with the aid of a qualified property and/or casualty insurance broker. Loss prevention and control services are also provided for workers' compensation and tort liability. As of July 1, 2011, the state's total insured property values were $17.8 billion.

## Small and Minority-Owned Business Assistance Program

The Small and Minority-Owned Business Assistance Program is responsible for supporting outreach to new, expanding and existing businesses unable to derive benefit from conventional means of monetary resources and insight provided by traditional lenders and financial advisors. The Program consists of two components: Loans and Program Services. The loans provided must be for a specific project, however, acceptable purposes for loan proceeds can include acquisition of machinery and equipment; working capital; supplies and materials; inventory and certain other business-related activity. Program Services include technical assistance, education and consulting services to facilitate support in the areas of strategy, planning and financial management. These Program components are deemed essential resources that will enable and enhance growth of the State's small business segment. The principal function of the Small and Minority-Owned Business Assistance Program is to provide a significant statewide platform through a support structure that fosters the expansion of small and minority-owned businesses.

## Tennessee Consolidated Retirement System

The Tennessee Consolidated Retirement System provides retirement coverage to state employees, higher education employees, teachers and employees of political subdivisions that have elected to participate in the plan. As of June 30, 2011, there were 219,914 active TCRS members: 42,142 state employees, 79,583 K-12 teachers, 81,780 political subdivision employees and 16,409 higher education employees. As of June 30, 2011, there were 117,185 retirees. TCRS paid $1.65 billion in benefits during fiscal year 2011. The state of Tennessee is responsible for the pension liability for state employees and higher education employees and funds a significant portion of the retirement liability for teachers through the BEP. Each participating political subdivision is responsible for the liability of its employees.

## Unclaimed Property Division

The Unclaimed Property Division administers the state's Uniform Disposition of Unclaimed Property Act. Under this act, the state provides one centralized location for the owners of abandoned property, or their heirs, to turn to when searching for checking accounts, savings accounts, insurance policies, utility deposits and securities. During the fiscal year, $71.5 million of unclaimed property was collected, which consisted of $60.1 million that was remitted to Treasury and $11.4 million in the sale of securities. In addition, $23.7 million was returned to owners or their heirs, local governments and other states. Since the program's inception in 1979, $747.6 million in unclaimed property has been reported to the Treasury and $246.2 million of that property has been returned to claimants.

# TREASURY NUMBERS AT A GLANCE FISCAL YEAR 2011

| | | | |
|---|---|---|---|
| **ADMINISTRATIVE** | Number of Filled Positions | | 211 |
| | Payroll Expenditures | $ | 15,553,400 |
| | Other Expenditures | $ | 6,481,900 |
| | Total Operating Expenditures | $ | 22,035,300 |
| **CASH MANAGEMENT PROGRAM** | General Fund Earnings | $ | 4,037,337 |
| | LGIP Earnings | $ | 8,630,649 |
| | Restricted Fund Earnings | $ | 5,271,358 |
| | Total Cash Management Earnings | $ | 17,939,344 |
| **RETIREMENT PROGRAM** | Retirement Benefits Paid to Retirees | $ | 1,652,871,076 |
| | Number of Retirees | | 117,185 |
| | Number of Active Members | | 219,914 |
| | Retirement Contributions Received | $ | 1,255,926,943 |
| | Retirement Net Investment Income | $ | 5,528,753,502 |
| **CLAIMS ADMINISTRATION PROGRAM** | Workers' Compensation Payments | $ | 26,380,151 |
| | Workers' Compensation Claims Filed | | 3,296 |
| | Employee Property Damage Payments | $ | 60,847 |
| | Employee Property Damage Claims Filed | | 132 |
| | Tort Payments | $ | 4,808,688 |
| | Tort Claims Filed | | 1,708 |
| | Criminal Injury Fund Payments | $ | 13,524,718 |
| | Criminal Injury Fund Claims Filed | | 5,905 |
| **RISK MANAGEMENT PROGRAM** | Estimated Gross Property Losses Incurred | $ | 14,870,605 |
| | Total Property Values Insured | $ | 17,888,235,300 |
| **CHAIRS OF EXCELLENCE PROGRAM** | Chairs of Excellence Investment Income | $ | 34,346,000 |
| | Chairs of Excellence Expenditures | $ | 6,905,984 |
| | Number of Chairs of Excellence | | 99 |
| **OTHER PROGRAMS** | Deferred Compensation Contributions | $ | 140,450,038 |
| | Deferred Compensation Accounts | | 80,668 |
| | Aggregate Deferred Compensation Balances | $ | 1,541,679,944 |
| | Flexible Benefits Plan Payments | $ | 7,964,291 |
| | Unclaimed Property Revenues | $ | 71,537,036 |
| | Unclaimed Property Payments | $ | 23,661,977 |
| | BEST Prepaid Accounts | | 8,830 |
| | BEST Prepaid Contributions (net of fees) | $ | 1,338,570 |
| | Optional Retirement Plan Contributions | $ | 81,160,085 |
| | Optional Retirement Plan Participants | | 11,562 |
| **FAIR VALUE OF ASSETS UNDER MANAGEMENT AT JUNE 30, 2011** | Retirement Trust Fund | $ | 33,663,308,244 |
| | Chairs of Excellence Trust Fund | $ | 243,105,645 |
| | State Pooled Investment Fund | $ | 7,467,791,379 |
| | Deferred Compensation (outside managers) | $ | 1,541,679,944 |
| | Optional Retirement Plan Assets (outside managers) | $ | 2,549,701,826 |
| | BEST Educational Services Plan | $ | 100,522,697 |
| | Total Assets Under Management | $ | 45,566,109,735 |

From 1929 – 1964, ***Shelby Farms*** was a penal farm, a place where prison inmates provided agricultural labor to supply food for inmates and sold overproduction on behalf of the state. The crops were bountiful and even produced a profit.

By 1970, the farm was declared surplus and Shelby County Government began evaluating proposals to sell the property for commercial, residential and office development. However, the community had already begun visiting Shelby Farms regularly to train dogs, ride horses, bird watch, run, hike, fish, picnic, etc. They were determined to protect Shelby Farms as a public park.

Currently, Shelby Farms Park is the largest urban park in the United States. Its 4,500 acres is home to more than 20 bodies of water, several paved, multi-use trails and primitive trails, the Lucius Burch Natural Area, the Agricenter International Expo Center, Showplace Arena, Farmer's Market, Catch'em Lake, a disc golf course, a kite-flying field and model airplane field, a playground, horse stables, paddle boats, pavilions, an amphitheater, a Visitor Center, a herd of American Bison, a dog park and more.

*Photo Credit: Baxter Buck*

The ***FedExForum*** opened September 4, 2004 in downtown Memphis on Beale Street. It is home to the Nation Basketball Association's Memphis Grizzlies and NCAA's University of Memphis Tigers. The Forum has played host to several big events, including the NCAA Tournament, WWE, UFC 107, boxing, concerts and more, generally seating more than 18,000. The Forum was the first venue in the NBA to use the see-through shot clock, allowing spectators to get a better view of the action.


Since Memphis is the "Home of the Blues" and the "Birthplace of Rock 'n' Roll", the FedExForum was designed with a music theme. The theme was meant to showcase the rich history of music and demonstrate the continuing production and development of new music in Memphis. As you walk through the Forum, you will see themed areas featuring the Blues and Rock 'n' Roll, along with a Gospel Zone, a unique Radio and Recording Zone, the Commercial Appeal Sun Studio Zone and the Memphis Music Today Zone featuring emerging artists in pop, rock, rap and hip-hop. Throughout the arena, guests can admire original art by regional artists whose work interprets music of the region. The theme continues in the naming of all concessions and restaurants. Even the restroom icons feature musical images.

*Photo Credit: Memphis Convention and Visitors' Bureau*

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

## Tennessee Consolidated Retirement System

The Tennessee Consolidated Retirement System (TCRS) was established July 1, 1972. Prior to this date, there were seven different public employee retirement systems. The TCRS, a defined benefit plan which is qualified under 401(a) of the Internal Revenue Code, is a retirement system for state employees, higher education employees, teachers and local government employees.

## Membership

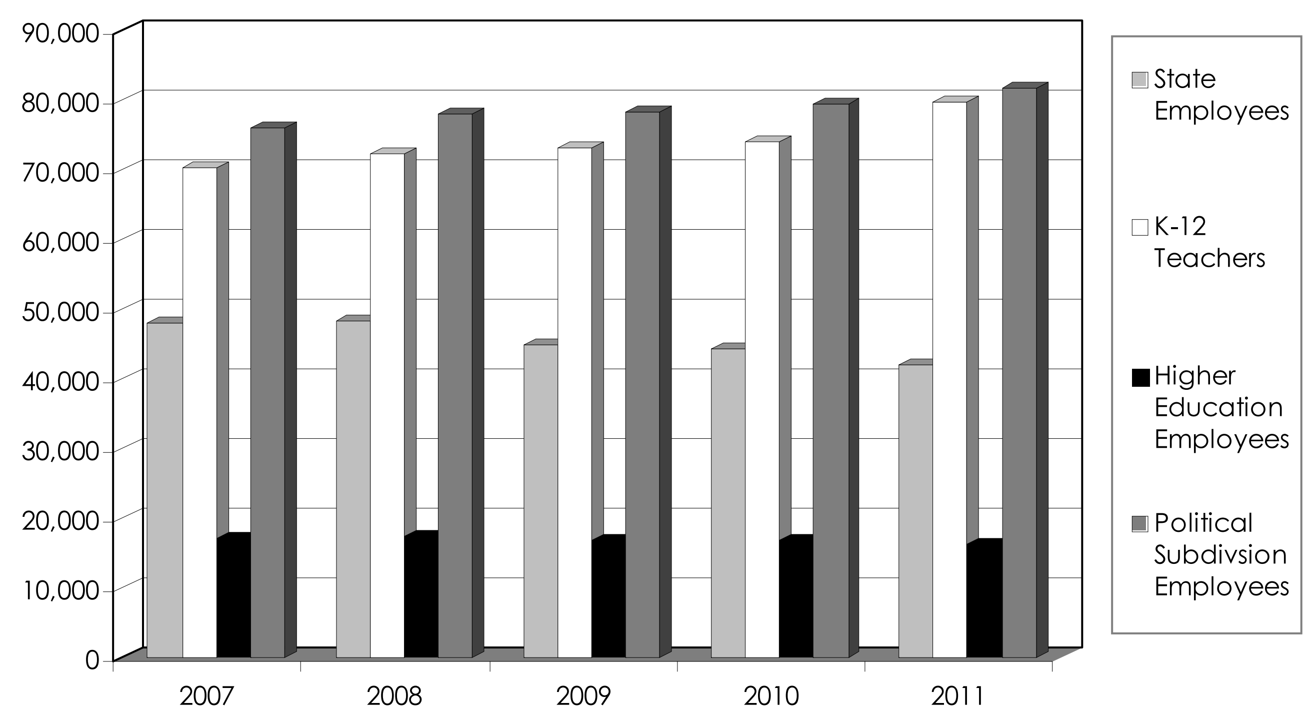
Membership in the retirement system is a condition of employment for full-time state employees, teachers, general employees in higher education and the employees of local governments that participate in TCRS. Membership is optional for certain part-time employees. Faculty employees in higher education may participate in either TCRS or an Optional Retirement Program (ORP), which is a defined contribution plan designed for faculty employees in institutions of higher education. An employee joining TCRS receives an introductory letter and membership pamphlet outlining various aspects of retirement membership.

State employees and teachers become vested after five years of service. Political subdivision members attain vested status upon completion of 10 years unless five year vesting has been authorized. A vested member is guaranteed a retirement benefit once the age requirements are met.

As of June 30, 2011, there were 219,914 active members of TCRS and 11,562 higher education employees participating in the ORP.

Since July 1, 1976, all new members of the TCRS except state judges have been classified as Group I members. State judges have been permitted to enroll in Group IV since September 1, 1990. From July 1, 1972 to June 30, 1976, all employees were classified as Group I, with the exception of state policemen, wildlife officers, firemen and policemen who were classified as Group II and judges and elected officials who were classified as Group III. Members of seven superseded systems are permitted to retain their original rights and benefits.

## *Active Members*
## *Fiscal Years 2007-2011*



# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

## CONTRIBUTIONS

The funding of retirement benefits is financed by member contributions, employer contributions and the earnings of the invested assets. Effective July 1, 1981, the employee contributions of certain state employees and higher education employees were assumed by the state. Local governments can also adopt these noncontributory provisions for their employees. Group I K-12 teachers and contributory local government employees contribute to TCRS at the rate of 5% of gross salary. Employee contribution rates vary for superseded classifications.

Effective January 1, 1987, all state employees and teachers who contribute a portion of their income to the retirement system became covered by Section 414(h) of the Internal Revenue Code. Under 414(h), payment of federal income tax on an employee's retirement contributions is deferred until these contributions are withdrawn in the form of a refund or monthly benefit payments. Political subdivisions may pass a resolution adopting Section 414(h) coverage for their employees.

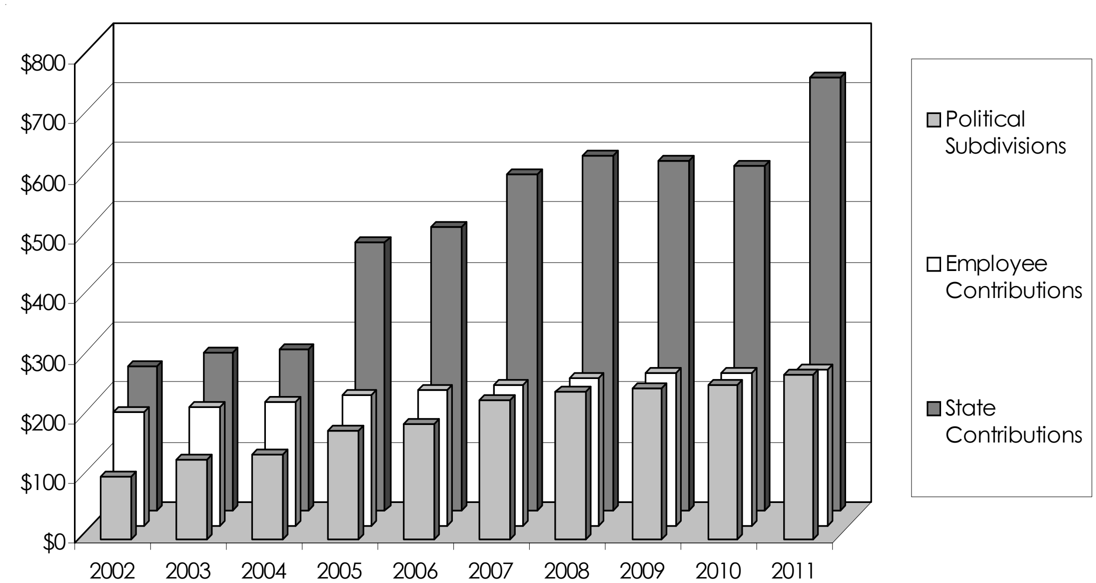
Upon termination of employment, a member may elect to withdraw his contributions and accumulated interest from the retirement system in a lump sum. By obtaining a lump sum refund, a member waives all rights and benefits in the retirement system. A vested member may leave his account balance in TCRS and apply for benefits upon meeting the age requirements. A non-vested member who terminates employment may only leave his account balance in TCRS for up to seven years. During the 2011 fiscal year, 4,500 refunds totaling $35.5 million were issued.

The contribution rate for the employers participating in the retirement system is determined by a biennial actuarial valuation performed by an independent actuarial firm. The contribution rates include funding for the basic benefit, the cost-of-living increase provisions and amortization of the accrued liability over a 40-year period which began in July of 1975. The employer contribution rates for the year ending June 30, 2011 were as follows:

| | |
|---|---|
| Noncontributory State and Higher Education Employees | 14.91% |
| K-12 Teachers | 9.05% |
| Political Subdivisions Individually-Determined Faculty Members Electing to Participate in the ORP | 10.0%* |

*11% for salary above the Social Security wage base.

## *RETIREMENT CONTRIBUTIONS FISCAL YEARS 2002-2011 EXPRESSED IN MILLIONS*



# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

## RETIREMENT BENEFITS

The benefits provided by TCRS are designed, when combined with the benefit payable from Social Security, to allow career employees to maintain their standard of living at retirement.

As of June 30, 2011, 117,185 retirees were receiving monthly benefit payments. This represents a 4.5% increase over the previous year.

Group I state employees and teachers become eligible to retire from the TCRS at age 60 with five years of service or at any age with 30 years of service. State employees and teachers become vested after five years of service. Political subdivision members attain vested status upon completion of 10 years unless five year vesting has been authorized. Retirement benefits are based on the average of the member's five highest consecutive years of salary and the years of creditable service. A reduced retirement benefit is available to vested members at age 55 or upon completion of 25 years of service.

A Group I benefits calculator is available on the program's Internet site: tcrs.tn.gov.

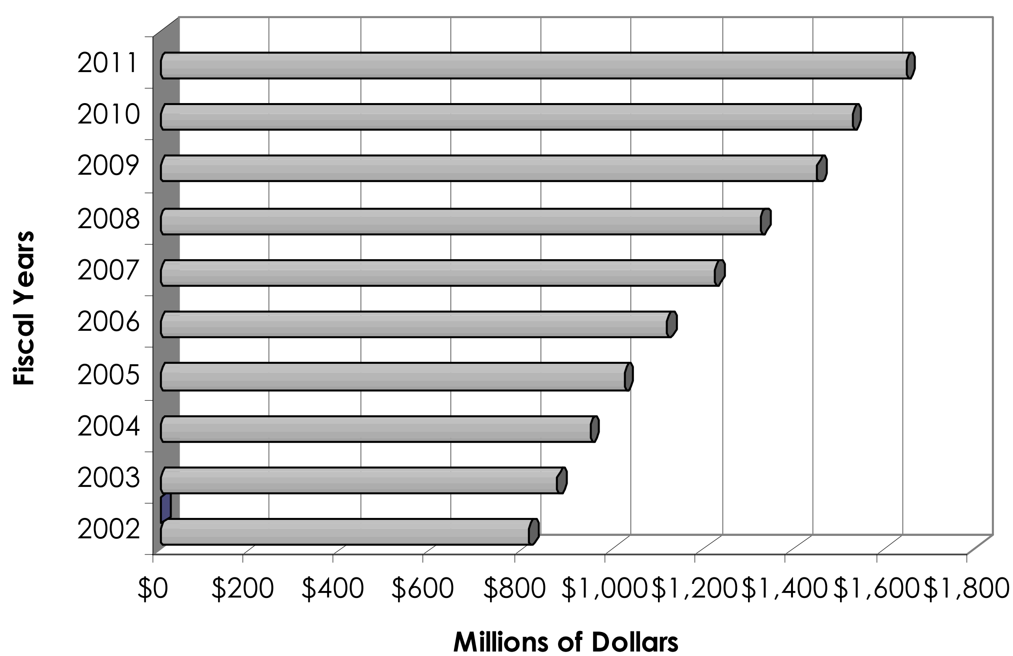
Disability benefits are available to active members with five years of service who become disabled and can not engage in gainful employment. There is no service requirement for disability benefits paid to active members whose disability is a result of an accident or injury occurring while the member was in the performance of duty.

Cost-of-living adjustments after retirement are based on the Consumer Price Index (CPI). If there is an increase in the CPI of as much as .5% in any calendar year, the retired member's benefit will be adjusted by an amount equal to the increase in the CPI, not to exceed 3% nor be less than 1%.

Certain death benefits are available to the beneficiary(s) of a member who dies prior to retirement. At retirement, a member may select an optional benefit that is actuarially reduced so that his beneficiary may continue to receive a benefit after his death.

Benefits paid in fiscal year 2011 totaled $1.65 billion, an increase of $117 million over 2010 benefit payments.

## ANNUAL BENEFIT PAYMENTS
### *FISCAL YEARS 2002-2011*
### *EXPRESSED IN MILLIONS*



# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

## TENNESSEE'S RETIREMENT PROGRAM, TCRS AND SOCIAL SECURITY BENEFITS *FOR CALENDAR YEAR 2011*

| Five-Year AFC* | Projected Annual Retirement Income | 15 Years Service | % of AFC | 20 Years Service | % of AFC | 25 Years Service | % of AFC | 30 Years Service | % of AFC | 35 Years Service | % of AFC |
|---|---|---|---|---|---|---|---|---|---|---|---|
| $15,000 | TCRS | $ 3,544 | | $ 4,725 | | $ 5,906 | | $ 7,088 | | $ 8,269 | |
| | Social Security | 9,420 | | 9,420 | | 9,420 | | 9,420 | | 9,420 | |
| | Total | $ 12,964 | 86.4% | $ 14,145 | 94.3% | $ 15,326 | 102.2% | $ 16,508 | 110.1% | $ 17,689 | 117.9% |
| $20,000 | TCRS | $ 4,725 | | $ 6,300 | | $ 7,875 | | $ 9,450 | | $ 11,025 | |
| | Social Security | 10,944 | | 10,944 | | 10,944 | | 10,944 | | 10,944 | |
| | Total | $ 15,669 | 78.3% | $ 17,244 | 86.2% | $ 18,819 | 94.1% | $ 20,394 | 102.0% | $ 21,969 | 109.8% |
| $25,000 | TCRS | $ 5,906 | | $ 7,875 | | $ 9,844 | | $ 11,813 | | $ 13,781 | |
| | Social Security | 12,456 | | 12,456 | | 12,456 | | 12,456 | | 12,456 | |
| | Total | $ 18,362 | 73.4% | $ 20,331 | 81.3% | $ 22,300 | 89.2% | $ 24,269 | 97.1% | $ 26,237 | 104.9% |
| $30,000 | TCRS | $ 7,088 | | $ 9,450 | | $ 11,813 | | $ 14,175 | | $ 16,538 | |
| | Social Security | 13,980 | | 13,980 | | 13,980 | | 13,980 | | 13,980 | |
| | Total | $ 21,068 | 70.2% | $ 23,430 | 78.1% | $ 25,793 | 86.0% | $ 28,155 | 93.9% | $ 30,518 | 101.7% |
| $35,000 | TCRS | $ 8,269 | | $ 11,025 | | $ 13,781 | | $ 16,538 | | $ 19,294 | |
| | Social Security | 15,492 | | 15,492 | | 15,492 | | 15,492 | | 15,492 | |
| | Total | $ 23,761 | 67.9% | $ 26,517 | 75.8% | $ 29,273 | 83.6% | $ 32,030 | 91.5% | $ 34,786 | 99.4% |
| $40,000 | TCRS | $ 9,450 | | $ 12,600 | | $ 15,750 | | $ 18,900 | | $ 22,050 | |
| | Social Security | 17,004 | | 17,004 | | 17,004 | | 17,004 | | 17,004 | |
| | Total | $ 26,454 | 66.1% | $ 29,604 | 74.0% | $ 32,754 | 81.9% | $ 35,904 | 89.8% | $ 39,054 | 97.6% |
| $45,000 | TCRS | $ 10,631 | | $ 14,175 | | $ 17,719 | | $ 21,263 | | $ 24,806 | |
| | Social Security | 18,528 | | 18,528 | | 18,528 | | 18,528 | | 18,528 | |
| | Total | $ 29,159 | 64.8% | $ 32,703 | 72.7% | $ 36,247 | 80.5% | $ 39,791 | 88.4% | $ 43,334 | 96.3% |
| $50,000 | TCRS | $ 11,813 | | $ 15,750 | | $ 19,688 | | $ 23,625 | | $ 27,563 | |
| | Social Security | 20,040 | | 20,040 | | 20,040 | | 20,040 | | 20,040 | |
| | Total | $ 31,853 | 63.7% | $ 35,790 | 71.6% | $ 39,728 | 79.5% | $ 43,665 | 87.3% | $ 47,603 | 95.2% |
| $55,000 | TCRS | $ 12,994 | | $ 17,325 | | $ 21,656 | | $ 25,988 | | $ 30,319 | |
| | Social Security | 21,336 | | 21,336 | | 21,336 | | 21,336 | | 21,336 | |
| | Total | $ 34,330 | 62.4% | $ 38,661 | 70.3% | $ 42,992 | 78.2% | $ 47,324 | 86.0% | $ 51,655 | 93.9% |
| $60,000 | TCRS | $ 14,199 | | $ 18,932 | | $ 23,664 | | $ 28,397 | | $ 33,130 | |
| | Social Security | 22,044 | | 22,044 | | 22,044 | | 22,044 | | 22,044 | |
| | Total | $ 36,243 | 60.4% | $ 40,976 | 68.3% | $ 45,708 | 76.2% | $ 50,441 | 84.1% | $ 55,174 | 92.0% |
| $65,000 | TCRS | $ 15,577 | | $ 20,769 | | $ 25,961 | | $ 31,154 | | $ 36,346 | |
| | Social Security | 22,752 | | 22,752 | | 22,752 | | 22,752 | | 22,752 | |
| | Total | $ 38,329 | 59.0% | $ 43,521 | 67.0% | $ 48,713 | 74.9% | $ 53,906 | 82.9% | $ 59,098 | 90.9% |
| $70,000 | TCRS | $ 16,955 | | $ 22,607 | | $ 28,258 | | $ 33,910 | | $ 39,561 | |
| | Social Security | 23,448 | | 23,448 | | 23,448 | | 23,448 | | 23,448 | |
| | Total | $ 40,403 | 57.7% | $ 46,055 | 65.8% | $ 51,706 | 73.9% | $ 57,358 | 81.9% | $ 63,009 | 90.0% |

* Average Final Compensation (AFC) is the average of the member's five highest consecutive years of salary.

This chart is based on a date of retirement in 2011. Social Security benefits have been calculated by Bryan, Pendleton, Swats & McAllister, actuarial consultants for the TCRS, utilizing the following assumptions:

(1) Retirement is taking place at age 65 in 2011;
(2) The retiree has worked a full career (TCRS plus other employers, if necessary) of 35 years or more; and
(3) Salary increases throughout the retiree's career have followed the same pattern as National Average Earnings.

The department's Internet benefits calculator allows members to receive an immediate estimate: tcrs.tn.gov

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

## ACTUARIAL VALUATION

An actuarial valuation of the TCRS is performed by an independent actuarial firm every two years. The purpose of the valuation is to determine the funding requirements for the employers participating in the TCRS. The latest valuation was performed July 1, 2009 to establish the employer contribution rates effective July 1, 2010. The system's accrued liability at July 1, 2009 was $3.6 billion. The state and teacher accrued liability is being amortized over a 20-year period. The amortization period for local governments varies by entity.

In addition to the biennial actuarial valuation, an experience study is conducted every four years for the purpose of establishing actuarial and economic assumptions to be used in the actuarial valuation process. Following are the assumptions used in the July 1, 2009 actuarial valuation of the plan:

***Economic Assumptions***

(1) 7.5% annual return on investments

(2) Graded salary scale reflecting plan experience

(3) 3.5% annual increase in Social Security wage base

***Actuarial Assumptions***

(1) Pre-Retirement mortality based on age and sex

(2) Post-Retirement mortality based on age

(3) Disability rate based on age

(4) Turnover rate based on age and length of service

(5) Retirement age distribution based on age and service

## POLITICAL SUBDIVISIONS

Political subdivisions may participate in the TCRS if the chief governing body passes a resolution authorizing coverage and accepting the liability associated with the coverage. Each political subdivision is responsible for the retirement cost of its employees and, in addition to employer contributions, pays the TCRS a fee for TCRS administration.

## POLITICAL SUBDIVISION PARTICIPATION

Participation as of June 30, 2011:

| | |
|---|---|
| Cities | 176 |
| Counties | 89 |
| Utility Districts | 66 |
| Special School Districts | 19 |
| Joint Ventures | 22 |
| Housing Authorities | 11 |
| 911 Emergency Communication Districts | 43 |
| Miscellaneous Authorities | 57 |
| Total | 483 |

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

## MAJOR LEGISLATIVE IMPROVEMENTS

**1972** Benefit formula improved from 1.12 percent of salary up to the SSIL to 1.5 percent of salary up to the SSIL.

**1973** Annual cost-of-living increase based on the CPI with a cap of 1.5 percent adopted for retirees.

**1974** Disability retirement eligibility requirement reduced from 10 years to 5 years of service.

Maximum annual cost-of-living increase raised to 3 percent.

Provision to increase retirees' benefits whenever the benefit formula is improved.

Service credit authorized for unused accumulated sick leave.

**1976** Service retirement eligibility requirements reduced from age 65 or 35 years of service to age 60 or 30 years of service.

Early retirement eligibility requirements reduced from age 60 or 30 years of service to age 55.

**1978** A bonus cost-of-living increase granted to retirees at a lump-sum cost of $15.3 million.

An optional retirement plan established for teachers in the Board of Regents system.

**1980** Death benefits for members dying in-service with 10 years of service improved by offering a 100 percent joint and survivor annuity of the member's accrued benefit for the spouse.

**1981** Noncontributory retirement for state employees and higher education employees adopted. Employees' contributions, up to 5 percent, were assumed by the state.

**1983** An actuarially reduced retirement benefit at any age with 25 years of service authorized.

**1984** Credit for out-of-state service for the purpose of determining retirement eligibility authorized.

Retirement credit for armed conflict approved.

Part-time employees permitted to participate in TCRS and members allowed to establish credit for previous part-time employment.

**1985** $22 million ad-hoc increase granted to retirees.

**1987** Service credit for half of peacetime military service made available.

$17 million ad-hoc increase granted to retirees.

Retirement incentive for state employees.

Section 414(h) of the IRC adopted, allowing employee contributions to be made on a tax-deferred basis.

**1990** Retirement incentive for state employees.

**1991** 3.6 percent indexing of salaries for noncontributory employees extended one year. Each succeeding year up to 1997, the 3.6 percent indexing was extended. In 1997, it was extended indefinitely.

**1992** Minimum number of years required to qualify for retirement was reduced from 10 to 5 years.

**1993** Salary portability for service in different classifications authorized effective January 1, 1994.

Benefit improvement up to 5 percent authorized.

**1997** Compounded COLA for retirees approved.

**1998** Group 2 and 3 service requirements amended to permit service retirement with 30 years of service, regardless of age.

Group 1 and Prior Class C benefit limitations increased to 80 percent.

Mandatory retirement established with supplemental bridge benefit for all state public safety officers.

**1999** Group 1 benefit maximum increased to 90 percent.

**2000** Group 2 benefit maximum increased to 80 percent.

**2001** Line of Duty Death Benefits adopted to guarantee a minimum $50,000 death benefit.

**2005** Return to work statutes were reformed, including a temporary employment increase to 120 days.

**2006** Ad-hoc increase granted to members retired prior to 1989.

**2007** Public Safety Officer benefits were enhanced.

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

## Optional Retirement Plan

The Optional Retirement Plan is a defined contribution plan. Investments are participant directed selected from options offered through the plan service providers using bundled contracts. Contributions to ORP for the year ended June 30, 2011 were $81.2 million and ORP assets were $2.55 billion. There were 11,562 ORP participants at June 30, 2011.

## Social Security

The Old Age & Survivors Insurance Agency (OASI) administers Section 218 of the federal Social Security Act for Tennessee public employees. This section relates to coverage agreements and modifications as well as to coverage determinations.

Prior to 1951, Social Security coverage was not available to public employees. Amendments to the Social Security Act made in 1950 allowed certain groups of state and local government employees who were not covered by an employer-sponsored retirement plan to voluntarily participate in Social Security. Amendments made in 1954 allowed coverage for public employees who were covered by an employer-sponsored retirement plan if federal referendum requirements are met.

The Tennessee Master Agreement was executed on August 16, 1951. It provided full Social Security coverage (retirement, survivors, disability and hospital insurance) to public employees who were not covered by an employer-sponsored retirement plan. A modification to the agreement, effective January 1, 1956, provided Social Security coverage to employees serving in positions which were then covered by the Tennessee State Retirement System and the Tennessee Teachers' Retirement System. After the Tennessee Consolidated Retirement System was established July 1, 1972, a statewide Social Security coverage referendum was held among eligible employees.

The 1985 Budget Reconciliation Act mandated Medicare hospital insurance coverage for public employees hired after March 31, 1986 who do not have full Social Security coverage. The Omnibus Budget Reconciliation Act of 1990 (OBRA) generally mandated full Social Security coverage for state and local government employees who are not covered by an employer-sponsored retirement plan.

Effective in 1991, separate wage bases were implemented for Social Security and Medicare and separate reporting of withholding was required.

## Schedule of Historical Social Security Contribution Rates

| Calendar Year | Employee Rate | Employer Rate | Social Security Wage Base | Medicare Wage Base |
|---|---|---|---|---|
| 2011 | 5.65% | 7.65% | $ 106,800 | No Limit |
| 2010 | 7.65% | 7.65% | 106,800 | No Limit |
| 2009 | 7.65% | 7.65% | 106,800 | No Limit |
| 2008 | 7.65% | 7.65% | 102,000 | No Limit |
| 2007 | 7.65% | 7.65% | 97,500 | No Limit |
| 2006 | 7.65% | 7.65% | 94,200 | No Limit |
| 2005 | 7.65% | 7.65% | 90,000 | No Limit |
| 2004 | 7.65% | 7.65% | 87,900 | No Limit |
| 2003 | 7.65% | 7.65% | 87,000 | No Limit |
| 2002 | 7.65% | 7.65% | 84,900 | No Limit |

# DEFERRED COMPENSATION PROGRAM

## Deferred Compensation Program

The Deferred Compensation Program is a voluntary program designed to provide state employees with the opportunity to accumulate supplemental retirement income on a tax advantaged basis. Participants may postpone income taxes on contributions and earnings by agreeing to defer receipt of a portion of their current income until retirement. In 2007, the 401(k) Plan began offering employees a designated Roth 401(k) after tax contribution option as payroll systems accommodated this change. The contributions are made after tax and the distributions are tax advantaged subject to timing restrictions.

This program offers employees two plans. The 457 plan was implemented in the 1981-82 fiscal year and the 401(k) plan was implemented in the 1983-84 fiscal year. In accordance with changes to Internal Revenue Code Section 457, the state's 457 plan was converted to a trust effective January 1, 1999.

As of June 30, 2011, accounts were held by 74,752 individuals in the 401(k) plan and 5,916 individuals in the 457 plan. At fiscal year end, 30,787 state employees, 11,315 University of Tennessee employees and 9,680 Tennessee Board of Regents employees were actively contributing to the 401(k) plan and 3,353 state employees, 648 University of Tennessee employees and 410 Tennessee Board of Regents employees were actively contributing to the 457 plan.

The program is used by state employees of all ages and salary levels. The majority of active contributors are under age 48 and earn below $35,000 per year.

IRS regulations for 2011 allow a maximum deferral in the 457 plan of 100% of compensation up to the maximum annual contribution of $16,500. The maximum deferral in the 401(k) plan is 100% of compensation up to the maximum annual contribution of $16,500. Participants who also use a 403(b) plan are subject to additional limits. Participants age 50 and older are eligible to make additional deferrals.

During the 2011 fiscal year, the state, the Tennessee Board of Regents and the University of Tennessee each matched their employees' contributions to the 401(k) plan at $50 per month as authorized by the General Assembly. The amount contributed by the state during the year was $30.5 million. Employees contributed $110 million.

Participants in the program at June 30, 2011 directed the investment of their deferred salary to the Regions Bank Time Deposit Account, Allianz NFJ Large Cap Institutional Fund, Calvert Income Fund, Columbia Acorn Z Fund, Columbia Midcap Value Z Fund, DFA International Value Fund, Fidelity Contra Fund, Fidelity International Discovery Fund, Fidelity OTC Portfolio Fund, Fidelity Puritan Fund, Fidelity Retirement Government Money Market, Fidelity Stock Selector Small Cap, ING Fixed Plus Account, Invesco Van Kampen Small Cap Growth Fund, Vanguard Institutional Index Fund, Vanguard Total Bond Market Index, and several options through the ING variable annuity. A self-directed brokerage account option provides access to additional mutual funds.

Enrollment and record keeping services for the program are provided by Great-West Retirement Services. The use of an unbundled arrangement enables participants to receive an objective presentation of the investment products, to avoid the sales fees traditionally associated with bundled products and to receive consolidated account statements and benefit estimates. All of the products available for new enrollment are offered without sales fees, surrender fees, mortality and expense risk fees or minimum deposit requirements.

Participants receive a quarterly statement showing their contributions and earnings during the quarter. In addition, once a year, participants receive a special statement projecting their account balance to a variety of retirement ages and showing the monthly income those account balances might provide. The program provides a variety of communication and education materials and services, including a comprehensive Internet site, a handbook for participants, several booklets on special topics, investment seminars around the state, plus a voice response telephone system and an Internet account access system which provide participants with immediate access to account balances and account transactions 24 hours a day. Online statements are available upon request.

The Internet site, www.tn.gov/treasury/dc, provides full information about the program. Information available through the site includes forms, participation information and illustrations, descriptions of the

## DEFERRED COMPENSATION PROGRAM

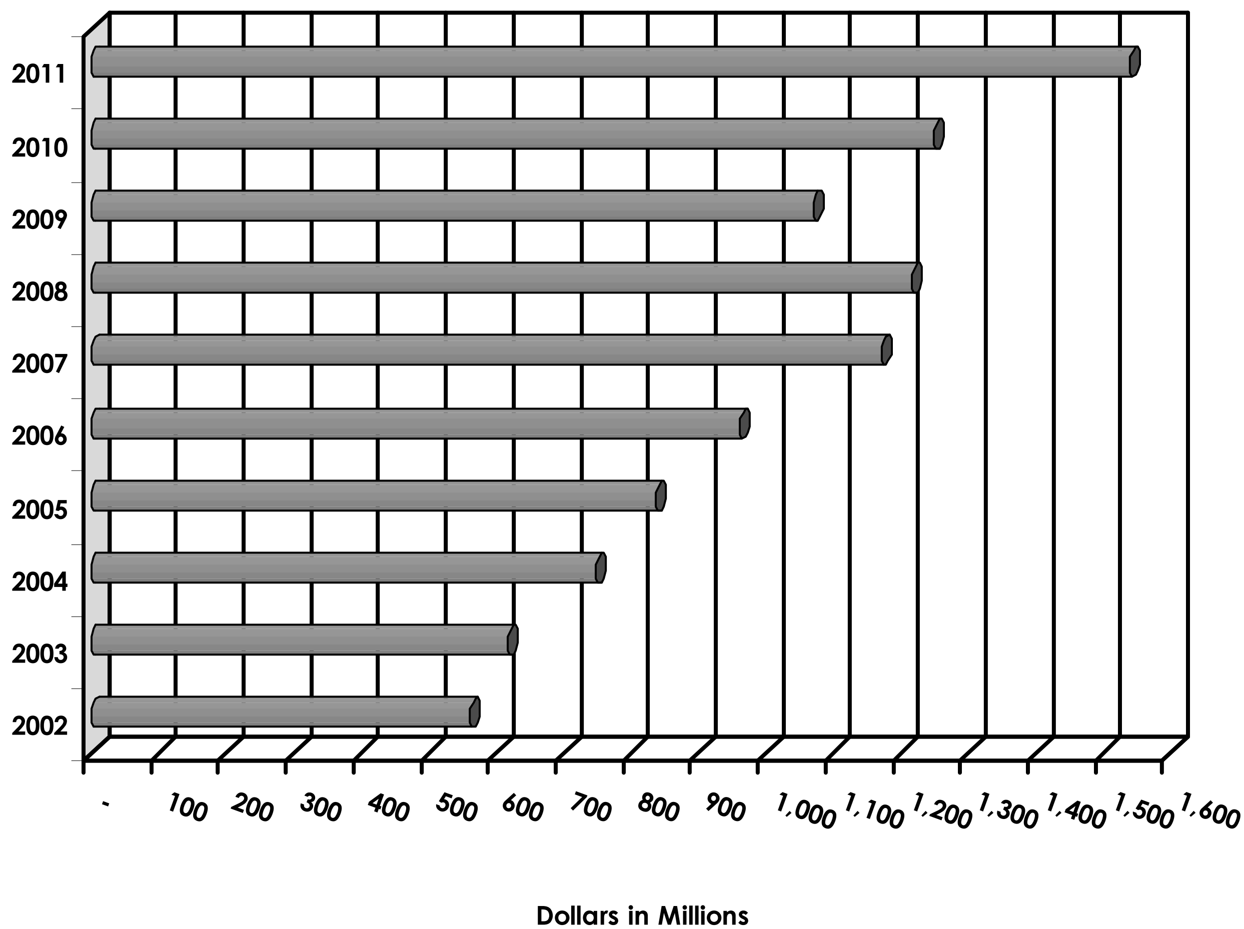
investment choices and historical performance figures, an interactive benefit calculator, complete information for participants who may be approaching retirement age or considering withdrawing funds from the program, an e-mail address for participants to request additional personalized information and full account activity access.

For the year ending June 30, 2011, contributions to the program totaled $140.5 million. Contributions are wired for immediate crediting. At June 30, 2011, accumulated account balances totaled $1.54 billion.

Under the loan program offered in the 401(k) plan, active employees who have accumulated $4,000 or more in their 401(k) account may borrow up to half of their account value. Participants repay principal and interest to their 401(k) account through salary deduction. Taxes continue to be deferred while funds accumulated in the plan are in loan status. As of June 30, 2011, there were 7,221 loans outstanding from the 401(k) plan. Outstanding loan balances totaled $23.4 million.

Benefits from the program may be distributed in periodic payments, in an annuity or in a lump sum. During the year ended June 30, 2011, there were 7,754 periodic payments made from the program. Members may choose monthly, quarterly, semi-annual or annual payments. In addition, 4,200 lump-sum distributions and 3,238 partial lump-sum distributions were issued during fiscal year 2011.

### DEFERRED COMPENSATION PROGRAM ASSETS
### *EXPRESSED IN MILLIONS*
### *FISCAL YEARS 2002-2011*



# DEFERRED COMPENSATION PROGRAM

## DEFERRED COMPENSATION CONTRIBUTIONS AND MARKET VALUE
## *FISCAL YEAR 2011*

| | Contributions FY 2010-2011 | Market Value June 30, 2011 |
|---|---|---|
| **Plan I (457)** | | |
| ING | $ 2,743,579 | $ 43,089,580 |
| American General | 9,743 | 505,061 |
| Calvert | 786,717 | 8,312,493 |
| Fidelity | 8,122,264 | 109,300,902 |
| State Street** | 909,484 | 0 |
| Regions | 1,477,545 | 19,398,380 |
| Vanguard | 3,163,212 | 23,483,637 |
| Dimenensional | 363,514 | 2,280,709 |
| TD Ameritrade SDB MM | 0 | 30,860 |
| TD Ameritrade SDB Securities Bal | 0 | 323,488 |
| | $ 17,576,058 | $ 206,725,110 |
| **Plan II (401K)** | | |
| ING | $ 18,674,438 | $ 212,021,063 |
| Calvert | 4,078,306 | 43,666,478 |
| Fidelity | 64,958,602 | 836,489,417 |
| State Street** | 5,078,824 | 0 |
| Regions | 11,441,892 | 109,598,125 |
| Vanguard | 10,864,040 | 119,418,471 |
| Dimensional | 1,771,462 | 12,255,630 |
| TD Ameritrade SDB MM | 0 | 328,130 |
| TD Ameritrade SDB Securities Bal | 0 | 1,682,579 |
| Loan Repayment | 6,006,416 | 0 |
| | $ 122,873,980 | $ 1,335,459,893 |
| **Total for Both Plans** | **$ 140,450,038** | **$ 1,542,185,003** |

**State Street SSgA fund was closed during fiscal year 2011 and all accounts were transferred to the Vanguard Institutional Index.

# FLEXIBLE BENEFITS PLAN

## Flexible Benefits Plan

The Flexible Benefits Plan is an optional benefit plan that enables state employees to pay for certain expenses with tax-free salary. Authorized under Section 125 of the Internal Revenue Code, this plan allows employees to avoid income tax and Social Security tax on the portion of the upcoming year's salary they agree to set aside for that year's (1) group medical insurance premiums, (2) group dental insurance premiums, (3) out-of-pocket medical expenses and (4) dependent care expenses.

In exchange for its favorable tax treatment, the plan must comply with specific rules set forth by the Internal Revenue Code and Regulations. Employees must decide what they will purchase through the plan and how much they will spend before the year begins. State employees enrolled in a group health or dental insurance program are automatically enrolled in the insurance premium portion of the plan. Use of the other benefit options requires a new election each year.

Enrollment in the plan is for a full calendar year. Enrollments may not be changed after the year has begun unless the employee experiences a change in family status and reports that change promptly. Employees must use the amounts set aside in each category for corresponding expenses incurred during the year and any amount not used by the employee must be subject to forfeiture.

Effective January 1, 2009, the Flexible Benefits Plan offers employees the opportunity to open transportation and parking flexible benefits accounts as authorized by Section 132 of the Internal Revenue Code. These accounts benefit employees by allowing them to designate an amount, up to the established limitations, to be withheld from their paychecks as a pre-tax benefit. These deductions are exempt from Federal Income and Social Security taxes. Participation in this program will result in the employee having a lower tax obligation during each calendar year in which they participate.

Unlike medical and dependent care flexible benefits accounts, there is no requirement for new employees to enroll within 30 days of being hired and there is no annual enrollment period for existing employees. An employee may enroll in a transportation account and/or a parking account at any time during employment. Transportation and parking flexible benefits accounts can be terminated at any time by the employee.

At June 30, 2011, over 38,000 state employees were enrolled in one or more of the plan's four Section 125 options: 38,546 employees used the plan to pay medical insurance premiums, 27,858 paid dental insurance premiums, 5,300 used the medical expense reimbursement account and 408 used the dependent care reimbursement account. In addition, 203 and 90 state employees participated in the parking and transportation reimbursement accounts, respectively.


***Elvis Aaron Presley*** was born in Tupelo, Mississippi, on January 8, 1935. His twin brother was stillborn, leaving Elvis to grow up as an only child. In 1948, he and his parents moved to Memphis.

In 1954, Elvis began his singing career with the legendary Sun Records label in Memphis. By 1956, he was an international sensation. His unique sound and style challenged the social and racial barriers of the time and he developed a new era of American music and popular culture.

His talent, good looks, sensuality, charisma and good humor endeared him to millions, as did the humility and human kindness he demonstrated throughout his life. Known the world over by his first name, he is regarded as one of the most important figures of twentieth century popular culture. Elvis died at his Memphis home, Graceland, on August 16, 1977.

*Photo Credit: State of Tennessee's Photographic Services*

At the Mud Island River Park, the ***River Walk*** is one of the most unique representations of the Mississippi River in the world. It is a 1/2 mile-long exact scale model of the lower Mississippi River flowing from its confluence with the Ohio River at Cairo, Illinois 954 miles south to the Gulf of Mexico.

Twenty cities are mapped along the Riverwalk. Along your journey, you will revisit historical events and learn about geographical transformations. The "1,000" mile journey concludes at the Gulf of Mexico, a one-acre enclosure that holds 1.3 million gallons of water. There, visitors can enjoy a leisurely pedal boat ride around the Gulf area with the Memphis skyline in the background.

*Photo Credit: Mud Island River Park*

# TCRS INVESTMENTS

## TCRS Investments

Investment objectives for the TCRS Investment Division are to obtain the highest available return on investments consistent with the preservation of principal, while maintaining sufficient liquidity to react to the changing environment and to pay beneficiaries in a timely manner.

TCRS Investment Division's policies and strategies serve to benefit plan members in several ways. The emphasis on a conservative asset allocation and high quality securities helps to ensure the soundness of the system and the ability to provide the needed funds upon a member's retirement.

Funds in the retirement system are actively managed with a diversified portfolio of high-quality domestic and international bonds, domestic and international stocks, real estate, private equity and money market instruments.

The investment authority for TCRS is set out in *Tennessee Code Annotated*, Section 8-37-104(a), which provides that, with certain specific exceptions, investments of TCRS assets are subject to the same terms, conditions, and limitations imposed on domestic life insurance companies. It further provides that the investment policy for TCRS funds is subject to the approval of the Board of Trustees. From time to time, the TCRS Investment Division engages outside investment managers to manage a limited number of asset classes or subclasses. Pursuant to *Tennessee Code Annotated*, Section 8-37-114, in any such procurement, the Investment Division invites emerging investment managers to be among those entities providing proposals. In the most recent outside investment manager procurement in 2009, no responsive proposals were submitted by emerging investment managers. During the fiscal year 2010-2011, no procurements for external investment managers occurred and no assets were under the control of emerging investment managers.

The Investment Advisory Council established in *Tennessee Code Annotated*, Section 8-37-108 provides policy guidance to the Board of Trustees and the investment staff. The current Advisory Council is comprised of senior investment professionals from within the State of Tennessee.

To assist in the fiduciary responsibility for managing the TCRS portfolio, Strategic Investment Solutions, Inc. serves as the general investment consultant for TCRS. The Townsend Group serves as the real estate investment consultant. Cambridge Associates serves as the private equity consultant to the fund.

Northern Trust Company is the Master Trust Bank for TCRS which provides safekeeping and accounting services for the investment portfolio.

## Cost of Investment Operation

The administrative cost to operate the investment program for TCRS is less than four basis points (.04%) of assets. The cost of four basis points includes the cost of personnel, operational cost, master bank custodian cost, record keeping and the cost of external management for international equities. Commission cost for trades are capitalized. Recent peer comparisons of investment management fees and expenses indicate the investment program is managed very cost effectively.

## Performance Measurement

An independent external investment consultant, Strategic Investment Solutions, Inc., provides performance measurement for TCRS. During the 2011 fiscal year, TCRS had a total return of 19.59%. Domestic stocks gained 33.71%, while the S&P 1500 Index gained 31.65%. Domestic bonds earned 6.00% versus the bond index benchmark of 5.91%. International stocks gained 33.01% versus 31.05% for the Morgan Stanley EAFE IMI Index. Real estate gained 15.50% versus a gain of 16.03% for the NCREIF index.

# TCRS INVESTMENTS

## INVESTMENT SUMMARY
### *AS OF JUNE 30, 2011*

| | Domestic | | International | | Total | |
|---|---|---|---|---|---|---|
| | Fair Value | % | Fair Value | % | Fair Value | % |
| Fixed Income | | | | | | |
| Government Bonds | $ 3,884,551,989 | 11.53% | $ 461,891,826 | 1.37% | $ 4,346,443,815 | 12.90% |
| Corporate Bonds | 3,764,807,282 | 11.16% | 0 | 0.00% | 3,764,807,282 | 11.16% |
| Municipal/Provincial Bonds | 149,480,502 | 0.44% | 0 | 0.00% | 149,480,502 | 0.44% |
| Total Bonds | 7,798,839,773 | 23.13% | 461,891,826 | 1.37% | 8,260,731,599 | 24.50% |
| Asset Backed | 1,128,915,635 | 3.35% | 0 | 0.00% | 1,128,915,635 | 3.35% |
| Commercial Mortgage Backed | 381,607,895 | 1.13% | 0 | 0.00% | 381,607,895 | 1.13% |
| Government Agencies | 311,472,197 | 0.93% | 85,742,015 | 0.25% | 397,214,212 | 1.18% |
| Government Mortgage Backed Securites | 3,666,933,923 | 10.87% | 0 | 0.00% | 3,666,933,923 | 10.87% |
| Non-Government CMOs | 313,391,359 | 0.93% | 0 | 0.00% | 313,391,359 | 0.93% |
| Govt Issued Commercial Mortgaged Backed | 4,990,660 | 0.01% | 0 | 0.00% | 4,990,660 | 0.01% |
| Guaranteed Fixed Income | 10,023,580 | 0.03% | 0 | 0.00% | 10,023,580 | 0.03% |
| Preferred Stock | 9,710,000 | 0.03% | 60,450,459 | 0.18% | 70,160,459 | 0.21% |
| Total Fixed Income | 13,625,885,022 | 40.41% | 608,084,300 | 1.80% | 14,233,969,322 | 42.21% |
| Common Stock | | | | | | |
| Consumer Discretionary | 1,221,775,375 | 3.62% | 639,459,182 | 1.90% | 1,861,234,557 | 5.52% |
| Consumer Staples | 1,073,674,980 | 3.18% | 405,760,018 | 1.20% | 1,479,434,998 | 4.38% |
| Energy | 1,397,152,907 | 4.13% | 749,182,214 | 2.23% | 2,146,335,121 | 6.36% |
| Financials | 1,638,328,684 | 4.86% | 1,351,616,095 | 4.01% | 2,989,944,779 | 8.87% |
| Healthcare | 1,389,187,706 | 4.12% | 438,375,068 | 1.30% | 1,827,562,774 | 5.42% |
| Industrials | 1,382,053,804 | 4.10% | 898,476,135 | 2.66% | 2,280,529,939 | 6.76% |
| Information Technology | 2,029,110,936 | 6.02% | 346,642,586 | 1.03% | 2,375,753,522 | 7.04% |
| Materials | 471,154,626 | 1.40% | 843,810,718 | 2.50% | 1,314,965,344 | 3.90% |
| Telecommunication Services | 293,760,927 | 0.87% | 224,169,630 | 0.66% | 517,930,557 | 1.54% |
| Utilities | 383,266,768 | 1.14% | 112,195,219 | 0.33% | 495,461,987 | 1.47% |
| Misc/Unclassified | | 0.00% | 508,268,247 | 1.51% | 508,268,247 | 1.51% |
| Equity Exchange Traded Fund | 12,492,000 | 0.04% | 16,785,736 | 0.05% | 29,277,736 | 0.09% |
| Total Common Stock | 11,291,958,713 | 33.48% | 6,534,740,848 | 19.38% | 17,826,699,561 | 52.86% |
| Short-Term Investments | | | | | | |
| Commercial Paper | 388,064,409 | 1.15% | 0 | 0.00% | 388,064,409 | 1.15% |
| Cash & Cash Equiv. Derivative-Options | 10,938 | 0.00% | 0 | 0.00% | 10,938 | 0.00% |
| Pooled Funds and Mutual Funds | 113,893,100 | 0.34% | 0 | 0.00% | 113,893,100 | 0.34% |
| Total Short Term Investments | 501,968,447 | 1.49% | | 0.00% | 501,968,447 | 1.49% |
| Real Estate | 1,085,563,917 | 3.22% | 0 | 0.00% | 1,085,563,917 | 3.22% |
| Private Equities | 74,635,798 | 0.22% | 0 | 0.00% | 74,635,798 | 0.22% |
| Total Investments | 26,580,011,897 | 78.82% | 7,142,825,148 | 21.18% | 33,722,837,045 | 100.00% |
| Short Term Investments Classified as Cash Equivalents | (501,957,509) | | 0 | | (501,957,509) | |
| Total Investments as Shown on the Statement of Plan Net Assets | $ 26,078,054,388 | | $ 7,142,825,148 | | $ 33,220,879,537 | |

This schedule classifies Canadian investments as domestic securities, convertible bonds as fixed income securities and preferred stock as fixed income securities. For investment purposes convertible bonds and preferred stock are considered equity securities. Accordingly, the asset allocation percentages in this schedule will vary from the investment consultant's asset allocation percentages.

# TCRS INVESTMENTS

## TCRS Investments Benchmark Analysis

| Fiscal Year | (1) Public Fund Index Median Total Return | (2) TCRS Total Return |
|---|---|---|
| 2011 | 21.6% | 19.6% |
| 2010 | 13.5% | 10.2% |
| 2009 | (17.9)% | (15.3)% |
| 2008 | (4.7)% | (1.2)% |
| 2007 | 14.1 % | 13.2 % |
| 2006 | 6.9 % | 6.9 % |
| 2005 | 9.4 % | 7.3 % |
| 2004 | 15.0 % | 9.3 % |
| 2003 | 3.7 % | 4.9 % |
| 2002 | (5.2)% | (1.9)% |

(1) This index most closely resembles the structure and objectives of TCRS.

(2) This is the time-weighted method used to calculate returns and is the most accurate way to measure performance.

## Summary of TCRS Earnings
### *Fiscal Years 2007-2011*

| Fiscal Year | TCRS Portfolio Earnings |
|---|---|
| 2011 | $ 5,528,753,502 |
| 2010 | 2,692,345,919 |
| 2009 | (4,858,486,179) |
| 2008 | (430,058,924) |
| 2007 | 3,791,403,651 |

# STATE CASH MANAGEMENT

## State Cash Management

The State of Tennessee receives revenues from many sources such as taxes, licenses, fees and the federal government. As these monies are collected, they are deposited into one of the more than 80 financial institutions in Tennessee that have contracted with the state to serve as depositories. Under the state Constitution, the state may not spend more money on its programs than it has collected in revenues. Consequently, at any point in time the state has a sizable sum of money collected but not yet spent. These monies are invested by the Treasury Department until needed to pay for state expenses, payroll or benefit program disbursements.

During the 2011 fiscal year, the average balance of short term investments in the Treasurer's Cash Management program was $6,956,325,472 per month and interest income of $17,939,345 was earned. This includes deposits in the Local Government Investment Pool administered by the Treasury Department.

The State Funding Board sets the investment policy for the state. The State Funding Board is composed of the Governor, Commissioner of Finance and Administration, Comptroller, Secretary of State and Treasurer. The foremost investment objective of the State Pooled Investment Fund is safety of principal, followed by liquidity and then yield.

The current investment policy for the State Pooled Investment Fund was established to follow SEC Rule 2a-7-like guidelines for a money market fund. The maximum maturity of any security can not exceed 397 days and the weighted average maturity must be 120 days or less.

Funds may be invested in collateralized certificates of deposit with authorized Tennessee financial institutions; bills, notes and bonds of the U.S. Treasury; other obligations guaranteed as to principal and interest by the U.S. or any of its agencies and repurchase agreements against obligations of the U.S. or its agencies. Securities underlying repurchase agreements must be book-entry and delivered to a third party custodian in the name of the State Treasurer. Funds may also be invested in prime commercial paper and prime banker's acceptances.

At June 30, 2011, investments had an average maturity of 111 days and an average weighted yield of .20%. The total balance in the State Pooled Investment Fund at June 30, 2011, $7,466,292,809 fair value, was allocated as follows: U.S. Treasury government and agency securities, 66.52%; overnight deposits, 12.73%; collateralized certificates of deposit, 9.23% and commercial paper, 11.52%.

## Administration of Authorized State Depository Accounts

The Cash Management Division is responsible for the administration of the state's bank accounts in Tennessee financial institutions designated as authorized state depositories. Taxpayers and state agencies can deposit certain tax funds due to the state directly to any Treasurer's account at any authorized state depository.

The four most significant functions of administering the accounts are: (1) authorizing the state depository to accept state funds; (2) cash concentration; (3) collateralizing deposits and (4) monitoring collateral and deposits. Financial institutions' requests to become authorized state depositories are received in Cash Management, reviewed and forwarded to the appropriate state officials for consideration and approval.

The Cash Management Division is responsible for the cash concentration and management of all state depository accounts. Cash Management staff inquire on the balances of bank accounts and concentrate available funds into the State operating account to meet liquidity and investment needs. Account balances are drawn to the floor and concentrated by Fed wire or Automated Clearinghouse (ACH) transactions. The account floor is the minimum amount required by the financial institution for that particular account to earn interest. All of these state accounts are interest bearing.

Changes in branch banking laws and bank ownership due to mergers and acquisitions have brought about a need to quickly identify the parent bank, holding company and affiliate trustee custodians for state depositories. The ability to access and update this information on a database enhances the ability to

## STATE CASH MANAGEMENT

monitor deposits and collateral based on appropriate bank ownership.

This same database is accessed for current account information, for balance inquiry and cash concentration. It automates the link from balance inquiry to cash concentration by generating an ACH transaction. This automation improves controls over cash balances. The account balance floors are automatically compared to the balances entered to calculate ACH transaction amounts.

### State Collateral Program

Collateral is required to secure state deposits held in authorized state depository institutions. Statute sets the required collateral level at a market value of 105 percent of the value of the deposit secured, less the amount secured by the Federal Deposit Insurance Corporation. However, if the state depository is operating with a capital-to-asset ratio of less than five percent, additional collateral with a market value of $100,000 is required. Alternatively, a financial institution may pledge collateral via the collateral pool. The types of investment instruments which are eligible to be pledged as collateral are listed in this report.

The state of the economy and the financial environment have increased the importance of monitoring collateral. Cash Management staff review collateral daily, weekly and monthly. Any collateral deficiencies at authorized state depository institutions are reported to the Funding Board monthly. Reasons for under-collateralization include market price volatility of the security pledged, unexpected high deposits to an account, interest accruals, capital-to-asset ratios falling below five percent and principal paydowns on asset backed securities that have been pledged as collateral.

Collateral is held by an authorized trustee custodian in the name of the State of Tennessee. Treasury staff must authorize the receipt, release and substitution of all collateral.

### Collateral Pool

The operation of a collateral pool for banks is authorized by Tennessee Code Annotated, Section 9-4-501, et seq. The Collateral Pool operates under the jurisdiction of the Collateral Pool Board, which is comprised of four bankers and three government members representing state and local government divisions. The Collateral Pool Board has established rules and procedures that provide a low amount of risk and a high degree of efficiency for participating institutions.

While participation in the Collateral Pool is voluntary, participation is subject to application to and approval by the Collateral Pool Board. The Board has established minimum financial performance levels for applicants which must be met to ensure that program risk is minimized.

All public funds held by a pool participant are collateralized based on a collateral target calculated each month by the participant. The collateral target is based on the aggregate average balance of all public funds for the month multiplied by the pledge percentage level assigned to the participant by the Board.

The Board has established three different collateral pledge levels: 115 percent, 100 percent and 90 percent. The pledge level is based on financial criteria set by the Collateral Pool Board with the financially strongest institutions being eligible for the lowest pledge level. In March 2009, the Collateral Pool Board voted to suspend the 90% pledge level until further notice. Under the Collateral Pool, should a financial institution default with insufficient collateral to cover public deposits, then the other financial institutions must make up the difference on a pro rata basis. Accordingly, public funds are not at risk in the Collateral Pool.

All collateral transactions for the pool are monitored and processed through the Treasury Department using uniform statewide procedures. In addition, Treasury Department staff monitors all pool activity through the monthly, quarterly and annual reports required to be submitted by pool participants or obtained from third party sources.

The Collateral Pool provides collateral for both state funds and local government funds for those institutions participating in the pool. The Collateral Pool serves as a significant administrative advantage for local governments. Under the Collateral Pool, the Treasurer, rather than the local government, is responsible for monitoring the pledge level; pricing collateral;

# STATE CASH MANAGEMENT

reconciling collateral monthly with the trustee custodian; monitoring collateral; pledging, releasing and substituting collateral and maintaining a trustee custodian relationship.

Currently, the Collateral Pool has 99 participant institutions collateralizing public funds in excess of $9.0 billion.

## STATE TRUST

The State Trust of Tennessee, a not-for-profit corporation chartered in the State of Tennessee in 1979, continues to be utilized to obtain check clearing services through the Federal Reserve Bank with a check redemption volume of 6,488,237 during fiscal year 2011 at an estimated savings of over $500,000.

## STATE CASH MANAGEMENT COMPARATIVE RETURNS

In order to ensure that state investment returns reflect current market conditions, several market indicators are carefully monitored. Among these are rates reported daily in the Wall Street Journal, rates on U.S. Treasury securities and institutional money market funds. The following table illustrates state returns compared with three of these indicators.

| Fiscal Year | (1) Total Pool Funds | (2) Merrill Lynch Institutional Fund | (3) Standard & Poor's 7-Day LGIP Yield Index | (4) 90-Day Treasury (CD Equivalent Yield) |
|---|---|---|---|---|
| 2011 | .26% | .16% | .14% | .11% |
| 2010 | .40% | .16% | .39% | .12% |
| 2009 | 1.66% | 1.67% | 1.33% | .64% |
| 2008 | 4.13% | 4.23% | 2.60% | 2.75% |
| 2007 | 5.30% | 5.11% | 4.50% | 5.02% |

(1) Investment return on total portfolio.

(2) This index most closely resembles the structures and objectives of the total cash portfolio.

(3) Index is for LGIP benchmark pools rated AAAm & AAm by S&P.

(4) This approximates the reinvestment yield for new funds for the period.

## Securities Acceptable as Collateral for State Deposits

1. U.S. Treasury Bills
2. U.S. Treasury Notes & Bonds
3. Federal Housing Administration (FHA) debentures
4. Government National Mortgage Associations (GNMA)*
5. Farm Credit System (FCS)
   a. Federal Land Bank Bond (FLBB)
   b. Farm Credit Systemwide Bonds (FCSB)
   c. Farm Credit Systemwide Discount Notes (FCDN)
   d. Farm Credit Systemwide Floating Rate Notes (FCFR)
6. Federal Home Loan Banks
   a. Bonds (FHLB)
   b. Discount Notes (FHDN)
   c. Floating Rate Notes (FHFR)
7. Federal Home Loan Mortgage Corporation (FHLMC)*
   a. Mortgage-Backed Participation Certificates and Adjustable Rate Securities (FMPC, FMAR)
   b. Discount Notes (FMDN)
8. Federal National Mortgage Association (FNMA)*
   a. Bonds, Debentures, Secondary Market Debt Obligations (FNSM)
   b. Discount Notes (FNDN)
   c. Floating Rate Notes (FNFR)
   d. Mortgage-Backed Pass-Through Certificates (FNRF)
   e. Residential Financing Securities (FNRF)
   f. Adjustable Rate Mortgage-Backed Bonds (FNAR)
9. Student Loan Marketing Association (SLMA)
   a. Discount Notes (SLDN)
   b. Fixed Rate Notes (SLMN)
   c. Floating Rate Notes (SLFR)
   d. Bonds (SLBD)
10. Tennessee Valley Authority Bonds and Notes (TVA)
11. Collateralized Mortgage Obligations (CMOs) and Real Estate Mortgage Investment Conduits (REMICs) that are direct obligations of a U.S. agency or FNMA/FHLMC, except that the "residual" class/tranche of such securities will not be acceptable. Sufficient excess securities should be pledged to allow for the periodic reduction of principal.
12. Certain Tennessee Municipal Bonds as specified in T.C.A. Section 9-4-103.
13. Surety Bonds issued by insurance companies meeting certain requirements, including licensure under the laws of Tennessee.
14. Standby Letters of Credit from approved Federal Home Loan Banks.

** Pass through securities must reflect current paid down values and be kept up to date.*

# STATE CASH MANAGEMENT

## Historical Analysis of State Cash Investments

***Collateralized Time Deposits***

| Fiscal Year | Average Amount Invested | Amount Earned | Rate of Return |
|---|---|---|---|
| 2011 | $ 772,436,583 | $ 2,478,112 | 0.33% |
| 2010 | 1,636,994,750 | 11,438,313 | 0.62% |
| 2009 | 2,618,880,250 | 47,806,706 | 1.82% |
| 2008 | 2,455,349,750 | 107,899,521 | 4.35% |
| 2007 | 2,124,406,667 | 112,695,354 | 5.30% |

***Repurchase Agreements and Overnight Deposit Accounts***

| Fiscal Year | Average Amount Invested | Amount Earned | Rate of Return |
|---|---|---|---|
| 2011 | $ 871,447,388 | $ 2,703,893 | 0.30% |
| 2010 | 643,502,305 | 1,061,207 | 0.30% |
| 2009 | 367,930,650 | 2,860,837 | 1.03% |
| 2008 | 387,890,324 | 12,631,202 | 3.93% |
| 2007 | 398,534,694 | 17,529,090 | 5.45% |

***Commercial Paper***

| Fiscal Year | Average Amount Invested | Amount Earned | Rate of Return |
|---|---|---|---|
| 2011 | $ 1,524,625,250 | $ 2,384,177 | 0.16% |
| 2010 | 1,302,143,334 | 2,167,028 | 0.17% |
| 2009 | 1,476,756,250 | 16,759,612 | 1.02% |
| 2008 | 2,481,205,417 | 92,953,120 | 3.87% |
| 2007 | 2,002,307,667 | 106,634,748 | 5.34% |

***U.S. Government Securities***

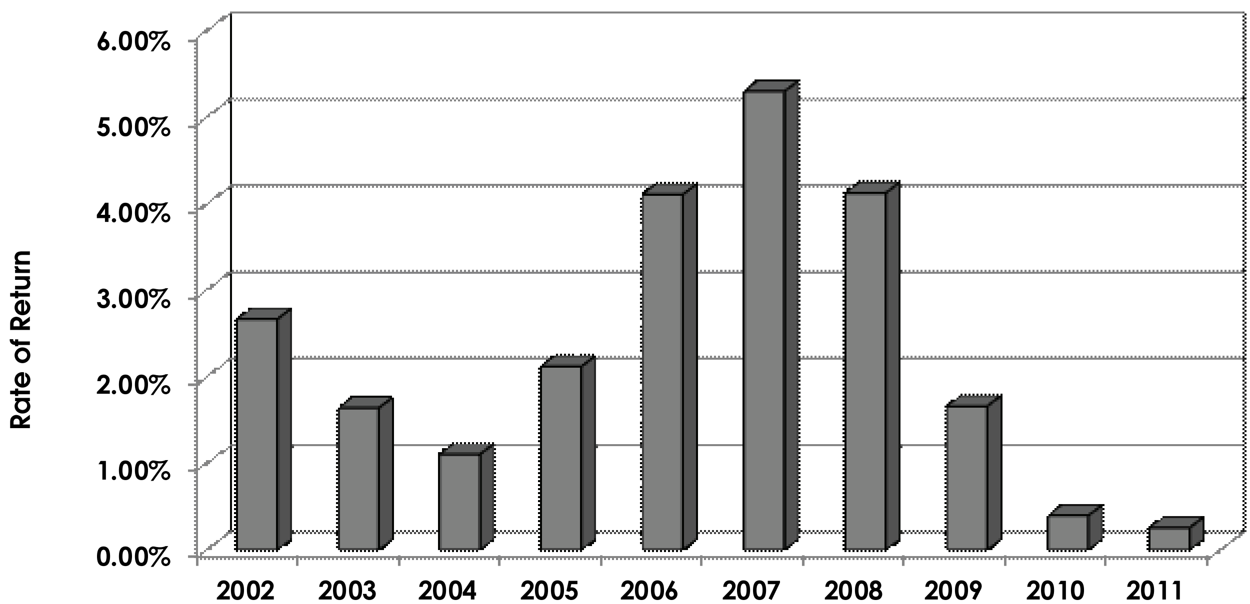
| Fiscal Year | Average Amount Invested | Amount Earned | Rate of Return |
|---|---|---|---|
| 2011 | $ 3,787,816,250 | $ 10,373,163 | 0.28% |
| 2010 | 3,284,981,083 | 12,298,843 | 0.38% |
| 2009 | 2,847,377,750 | 52,443,415 | 1.89% |
| 2008 | 2,774,037,333 | 112,693,789 | 4.22% |
| 2007 | 2,210,772,500 | 115,043,989 | 5.26% |

***Total Funds***

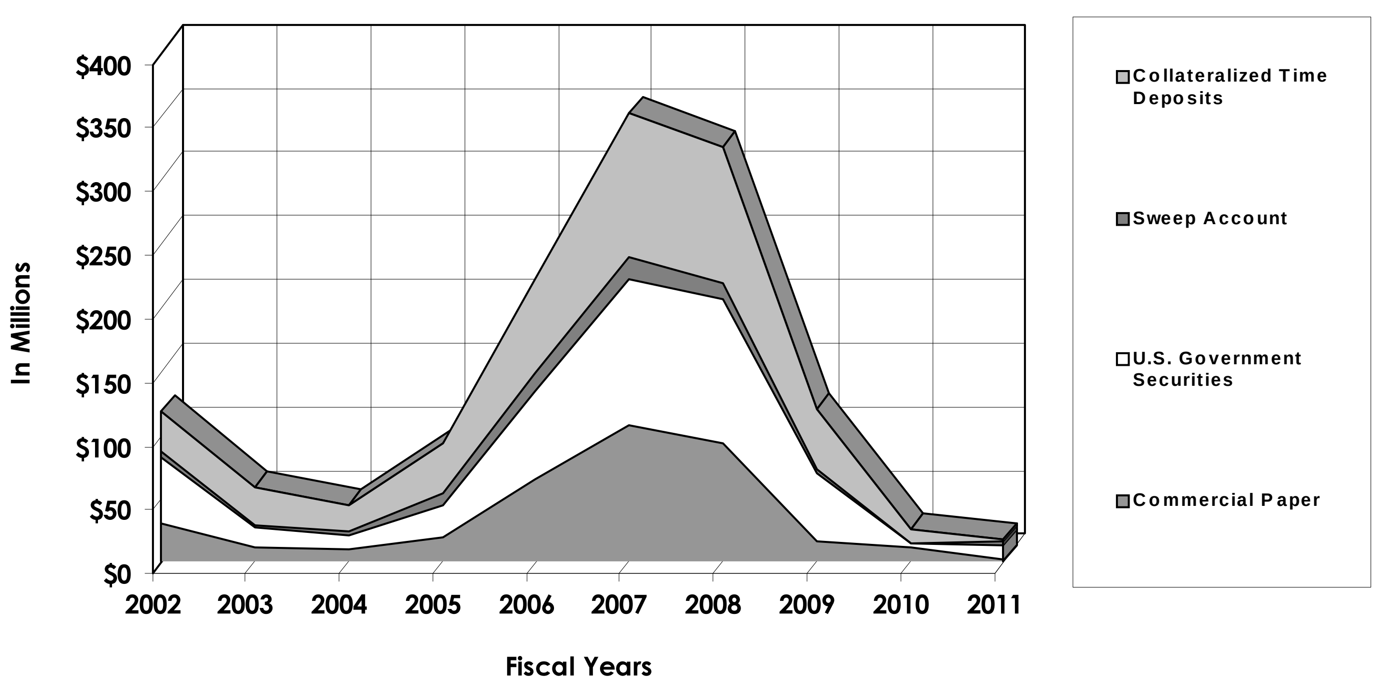
| Fiscal Year | Average Total Funds Invested | Cash Management Investment Earnings | Composite Weighted Average Rate of Return |
|---|---|---|---|
| 2011 | $ 6,956,325,471 | $ 17,939,345 | 0.26% |
| 2010 | 6,867,621,472 | 26,965,391 | 0.40% |
| 2009 | 7,310,944,900 | 119,870,570 | 1.66% |
| 2008 | 8,098,482,824 | 326,177,632 | 4.13% |
| 2007 | 6,736,021,528 | 351,903,181 | 5.30% |

## STATE CASH MANAGEMENT

### CASH MANAGEMENT INVESTMENTS COMPOSITE WEIGHTED AVERAGE RATE OF RETURN
### *FISCAL YEARS 2002-2011*




### ANALYSIS OF STATE CASH EARNINGS
### *FISCAL YEARS 2002-2011*



# STATE CASH MANAGEMENT

## CASH MANAGEMENT PORTFOLIO ANALYSIS
## *FISCAL YEAR ENDED JUNE 30, 2011*

| Date | Current Investment Yield | Total Portfolio Yield | Average Days to Maturity | Portfolio Composition: Certificates of Deposit | Sweep | U.S. Treasury Notes | U.S. Agency | Commercial Paper |
|---|---|---|---|---|---|---|---|---|
| July, 2010 | 0.17% | 0.29% | 86 | 12.68% | 11.03% | 0.00% | 53.44% | 22.85% |
| August, 2010 | 0.17% | 0.30% | 80 | 12.53% | 11.26% | 5.21% | 48.41% | 22.59% |
| September, 2010 | 0.17% | 0.30% | 86 | 13.00% | 12.13% | 5.30% | 47.35% | 22.22% |
| October, 2010 | 0.18% | 0.28% | 76 | 12.28% | 12.16% | 0.00% | 51.46% | 24.10% |
| November, 2010 | 0.18% | 0.28% | 71 | 12.28% | 13.66% | 0.00% | 48.22% | 25.84% |
| December, 2010 | 0.17% | 0.28% | 73 | 12.61% | 10.76% | 4.57% | 51.48% | 20.58% |
| January, 2011 | 0.15% | 0.26% | 72 | 11.10% | 11.58% | 9.52% | 45.44% | 22.36% |
| February, 2011 | 0.14% | 0.25% | 66 | 10.15% | 12.07% | 9.21% | 48.48% | 20.09% |
| March, 2011 | 0.12% | 0.23% | 62 | 8.84% | 10.91% | 9.98% | 49.22% | 21.05% |
| April, 2011 | 0.07% | 0.22% | 85 | 8.86% | 10.14% | 11.50% | 48.94% | 20.56% |
| May, 2011 | 0.07% | 0.19% | 90 | 9.19% | 10.21% | 11.25% | 49.40% | 19.95% |
| June, 2011 | 0.08% | 0.19% | 90 | 8.97% | 10.32% | 12.00% | 48.55% | 20.16% |
| Average | 0.14% | 0.26% | 78 | 11.04% | 11.35% | 6.54% | 49.20% | 21.87% |

| Month | General Fund Average | General Fund Percent | LGIP Average | LGIP Percent | Other Restricted Average | Other Restricted Percent | Total Average Invested |
|---|---|---|---|---|---|---|---|
| July 2010 | $2,105,071,217 | 29.59% | $3,114,283,727 | 43.78% | $1,893,691,020 | 26.62% | $7,113,045,964 |
| August 2010 | 2,225,732,953 | 31.53% | 2,981,956,889 | 42.24% | 1,851,963,989 | 26.23% | 7,059,653,831 |
| September 2010 | 2,130,017,153 | 30.78% | 2,862,750,204 | 41.36% | 1,928,442,619 | 27.86% | 6,921,209,976 |
| October 2010 | 2,332,891,230 | 33.61% | 2,927,237,917 | 42.18% | 1,680,196,684 | 24.21% | 6,940,325,831 |
| November 2010 | 1,857,321,600 | 28.48% | 2,959,662,010 | 45.38% | 1,705,217,861 | 26.14% | 6,522,201,471 |
| December 2010 | 1,614,569,895 | 25.32% | 3,101,454,761 | 48.64% | 1,660,666,511 | 26.04% | 6,376,691,167 |
| January 2011 | 1,807,904,403 | 25.92% | 3,562,733,277 | 51.08% | 1,603,670,796 | 22.99% | 6,974,308,476 |
| February 2011 | 1,657,626,210 | 23.28% | 3,774,651,555 | 53.01% | 1,688,293,163 | 23.71% | 7,120,570,928 |
| March 2011 | 1,771,243,441 | 23.86% | 4,352,864,304 | 58.64% | 1,299,274,070 | 17.50% | 7,423,381,815 |
| April 2011 | 2,056,564,823 | 27.20% | 4,127,247,476 | 54.59% | 1,376,330,183 | 18.21% | 7,560,142,482 |
| May 2011 | 2,581,444,739 | 33.02% | 3,816,356,572 | 48.81% | 1,420,366,704 | 18.17% | 7,818,168,015 |
| June 2011 | 2,606,157,437 | 32.72% | 3,589,853,828 | 45.07% | 1,769,106,235 | 22.21% | 7,965,117,500 |
| **Average** | $2,062,212,092 | 28.84% | $3,430,921,043 | 47.99% | $1,656,434,986 | 23.17% | $7,149,568,121 |

# STATE CASH MANAGEMENT

## LOCAL GOVERNMENT INVESTMENT POOL

Tennessee municipalities, counties, school districts, utility districts, community service agencies, local government units, and political subdivisions can deposit monies with the Treasurer to be invested in the state cash management investment pool. Of course, these local governments can invest their monies directly in the money market if they so desire. However, by allowing their dollars to be invested by the state they eliminate the complexities of managing day-to-day investment and collateral relationships with banks and/or securities dealers. This allows cash managers who have previously been limited either by the relatively small amount of funds available for investment or the complexities of today's investment environment to take advantage of the volume and expertise of the Treasurer's cash management program.

The Local Government Investment Pool began operations in November of 1980. Participation in the LGIP program currently stands in excess of 2,600 accounts. The Department of Transportation (DOT) program has more than 750 active accounts.

Local governments which enter into agreements with the DOT often establish an LGIP account to fund the local matching portion of a highway project grant. These DOT accounts are available to provide the local match to the specific highway project in a timely manner while earning interest for the local government. In a similar fashion, the Tennessee Board of Regents schools provide their matching portion of Capital Projects funds while earning interest for the benefit of the Board of Regents school.

An electronic banking system allows participants to access their accounts in a secure Internet application. Thus, participants are able to communicate their instructions by telephone, telefax, or the Internet.

In addition, voice mail telephone service has been provided to permit LGIP participants to give telephone transaction instructions while staff is busy on other telephone lines. Voice mail permits an increase in productivity while holding costs constant.

LGIP reports to participants are available online, including monthly statements and transaction confirmations. Monthly statements detail all debits and credits to the account during the month, the account's average daily balance, and interest credited. A transaction confirmation is available to the participant each time a deposit or withdrawal is made. Many participants rely on this documentation for daily and weekly reconciliations.

Participants earn interest on LGIP deposits based on the total portfolio return of the cash management pool, less a monthly administrative fee of five one hundredths of one percent (.05%). During the 2011 fiscal year, the average rate participants earned on their deposits after the fee reduction was .21%. Other activity is shown on the following schedule by participant group.

## LOCAL GOVERNMENT INVESTMENT POOL SCHEDULE OF ACTIVITY BY ENTITY TYPE
### *FISCAL YEAR ENDED JUNE 30, 2011*

| | Account Balance 6/30/2010 | Net Deposits/(Withdrawals) FY 2010-2011 | Interest Credited FY 2010-2011 | Account Balance 6/30/2011 |
|---|---|---|---|---|
| Cities | $ 1,121,672,669 | $ (73,457,053) | $ 2,115,376 | $ 1,050,330,992 |
| Counties | 527,250,053 | (43,971,204) | 1,127,901 | 484,406,750 |
| Commitments to D.O.T. | 42,683,497 | 3,544,830 | 90,588 | 46,318,915 |
| Educational Institutions | 825,860,760 | 186,791,674 | 2,058,379 | 1,014,710,813 |
| Bond Finance | 165,508,449 | 91,678,677 | 543,646 | 257,730,772 |
| Other | 438,642,793 | 53,806,418 | 2,694,759 | 495,143,970 |
| **Total** | **$3,121,618,221** | **$218,393,342** | **$ 8,630,649** | **$3,348,642,212** |

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM LARGEST HOLDINGS

## LARGEST STOCK HOLDINGS
### *AS OF JUNE 30, 2011*
### *BY FAIR VALUE*

| Shares | Security Name | Fair Value |
|---|---|---|
| 4,573,023 | Exxon Mobil Corp Com | $ 372,152,612 |
| 902,794 | Apple Inc Com Stk | 303,040,862 |
| 1,407,500 | International Business Machs Corp Com | 241,456,625 |
| 2,104,930 | Chevron Corp Com | 216,471,001 |
| 10,372,846 | General Electric Co | 195,631,876 |
| 7,312,450 | Microsoft Corp Com | 190,123,700 |
| 2,803,300 | Johnson & Johnson Com Usd1 | 186,475,516 |
| 4,513,275 | JP Morgan Chase & Co Com | 184,773,479 |
| 7,987,966 | Pfizer Inc Com | 164,552,100 |
| 4,727,400 | Oracle Corp Com | 155,578,734 |

## LARGEST BOND HOLDINGS
### *AS OF JUNE 30, 2011*
### *BY FAIR VALUE*

| Par Value | Security Name | Yield | Maturity | Moody's Rating | Fair Value |
|---|---|---|---|---|---|
| $ 235,900,000 | United States Treasury Infl Index Note | 2.15% | 01/15/16 | Aaa | $ 297,027,109 |
| 199,100,000 | United States Treasury Infl Index Bond | 3.16% | 01/15/26 | Aaa | 246,462,087 |
| 174,750,000 | United States Treasury Note | 2.11% | 02/15/21 | Aaa | 182,217,767 |
| 120,000,000 | United States Treasury Infl Index Note | 2.51% | 01/15/14 | Aaa | 157,326,268 |
| 155,350,000 | United States Treasury Bond | 3.57% | 05/15/41 | Aaa | 155,107,654 |
| 100,000,000 | United States Treasury Infl Index Bond | 2.53% | 01/15/25 | Aaa | 137,108,943 |
| 139,500,000 | United States Treasury Note | 2.09% | 11/15/20 | Aaa | 134,355,938 |
| 74,550,000 | United States Treasury Infl Index Bond | 2.95% | 04/15/32 | Aaa | 124,934,732 |
| 117,000,000 | United States Treasury Note | 3.27% | 01/15/21 | Aaa | 124,888,234 |
| 90,000,000 | United States Treasury Infl Index Note | 2.51% | 01/15/12 | Aaa | 116,437,957 |

*A complete portfolio listing is available upon request.*

Key to Ratings: All ratings presented are from Moody's Investors Service with the exception of some of the government agency securities. Moody's does not rate these securities. Standard & Poor's does provide ratings for the securities (AAA is Standard & Poor's highest rating). Government Securities are not rated per se' but are considered the best quality securities.

Moody's rates securities as follows:

| | |
|---|---|
| Aaa | Best Quality |
| Aa | High Quality |
| A | Upper Medium Quality |
| Baa | Medium Quality |
| NR | Not Rated |

# STATE CASH PORTFOLIO
# AS OF JUNE 30, 2011

| Description | Maturity | Yield to Maturity | Par Value | Fair Value |
|---|---|---|---|---|
| **U.S. TREASURY AND AGENCY OBLIGATIONS** | | | | |
| FAMC | 08/31/11 | 0.35% | $ 50,000,000 | $ 50,020,500 |
| FAMC | 10/25/11 | 0.26% | 50,000,000 | 49,993,500 |
| FAMC | 11/30/11 | 0.31% | 50,000,000 | 49,985,000 |
| FAMC | 02/29/12 | 0.23% | 50,000,000 | 49,959,500 |
| FAMC | 06/06/12 | 0.21% | 13,000,000 | 12,975,430 |
| FAMC | 06/20/12 | 0.25% | 50,000,000 | 49,901,500 |
| Federal Home Loan Bank | 05/15/12 | 0.29% | 37,000,000 | 37,288,230 |
| Federal Home Loan Bank | 04/27/12 | 0.41% | 100,000,000 | 100,009,000 |
| Federal Home Loan Bank | 04/13/12 | 0.21% | 48,000,000 | 48,730,080 |
| Federal Home Loan Bank | 05/18/12 | 0.28% | 53,855,000 | 54,237,909 |
| Federal Home Loan Bank | 07/27/11 | 0.18% | 50,000,000 | 49,999,500 |
| Federal Home Loan Bank | 07/29/11 | 0.18% | 50,000,000 | 49,999,000 |
| Federal Home Loan Bank | 08/15/11 | 0.07% | 64,000,000 | 63,998,080 |
| FFCB Discount Notes | 04/25/12 | 0.26% | 50,000,000 | 49,984,000 |
| FFCB Discount Notes | 06/22/12 | 0.22% | 75,000,000 | 74,972,250 |
| FFCB Discount Notes | 12/16/11 | 0.32% | 43,000,000 | 42,981,940 |
| FFCB Discount Notes | 09/30/11 | 0.35% | 25,000,000 | 25,015,500 |
| FFCB Discount Notes | 11/01/11 | 0.32% | 50,000,000 | 50,036,500 |
| FFCB Discount Notes | 11/30/11 | 0.28% | 50,000,000 | 50,037,000 |
| FFCB Discount Notes | 01/31/12 | 0.40% | 50,000,000 | 50,046,000 |
| FFCB Discount Notes | 03/22/12 | 0.40% | 25,000,000 | 25,016,250 |
| FHLMC .080 | 10/14/11 | 0.08% | 67,000,000 | 66,991,960 |
| FHLMC .110 | 12/15/11 | 0.11% | 67,000,000 | 66,971,860 |
| FHLMC .200 | 06/15/12 | 0.20% | 50,000,000 | 49,903,000 |
| FHLMC Note .055 | 08/15/11 | 0.06% | 152,726,000 | 152,721,418 |
| FHLMC Note .070 | 09/07/11 | 0.07% | 53,000,000 | 52,996,820 |
| FHLMC Note .070 | 10/14/11 | 0.07% | 121,000,000 | 120,985,480 |
| FHLMC Note .140 | 10/24/11 | 0.14% | 50,000,000 | 49,993,500 |
| FHLMC Note .140 | 12/06/11 | 0.14% | 20,800,000 | 20,791,680 |
| FHLMC Note .140 | 07/15/11 | 0.14% | 189,000,000 | 188,998,110 |
| FHLMC Note .145 | 08/10/11 | 0.15% | 50,000,000 | 49,999,000 |
| FHLMC Note .150 | 08/15/11 | 0.15% | 50,000,000 | 49,998,500 |
| FHLMC Note .150 | 08/29/11 | 0.15% | 50,000,000 | 49,998,500 |
| FHLMC Note .244 | 06/15/12 | 0.24% | 18,000,000 | 18,246,240 |
| FHLMC Note .249 | 06/15/12 | 0.25% | 57,940,000 | 58,732,619 |
| FHLMC Note .250 | 09/15/11 | 0.25% | 100,000,000 | 99,994,000 |
| FHLMC Note .255 | 06/15/12 | 0.26% | 82,797,000 | 83,929,663 |
| FHLMC Note 1.125 | 04/25/12 | 0.30% | 72,605,000 | 73,087,823 |

*(continued)*

# STATE CASH PORTFOLIO
# AS OF JUNE 30, 2011

| Description | Maturity | Yield to Maturity | Par Value | Fair Value |
|---|---|---|---|---|
| FHLMC Note 1.125 | 07/27/12 | 0.27% | $ 50,000,000 | $ 50,398,000 |
| FHLMC Note 1.125 | 07/27/12 | 0.27% | 50,000,000 | 50,398,000 |
| FNMA Discount Notes | 06/22/12 | 0.26% | 45,414,000 | 45,821,364 |
| FNMA Discount Notes | 06/22/12 | 0.25% | 38,796,000 | 39,144,000 |
| FNMA Discount Notes | 05/07/12 | 0.22% | 50,000,000 | 50,397,500 |
| FNMA Discount Notes | 07/30/12 | 0.26% | 20,514,000 | 20,687,138 |
| FNMA Discount Notes | 04/20/12 | 0.27% | 28,083,000 | 28,435,722 |
| FNMA Discount Notes | 08/08/11 | 0.30% | 131,000,000 | 130,997,380 |
| FNMA Discount Notes | 10/12/11 | 0.14% | 50,000,000 | 49,994,500 |
| FNMA Discount Notes | 10/12/11 | 0.14% | 100,000,000 | 99,989,000 |
| FNMA Discount Notes | 10/12/11 | 0.14% | 50,000,000 | 49,994,500 |
| FNMA Discount Notes | 11/15/11 | 0.12% | 66,000,000 | 65,982,180 |
| FNMA Discount Notes | 08/15/11 | 0.14% | 29,000,000 | 28,999,130 |
| FNMA Discount Notes | 09/15/11 | 0.12% | 50,000,000 | 49,997,000 |
| FNMA Discount Notes | 12/01/11 | 0.13% | 75,000,000 | 74,971,500 |
| FNMA Discount Notes | 07/01/11 | 0.29% | 40,549,000 | 40,549,000 |
| FNMA Discount Notes | 08/01/11 | 0.26% | 67,632,000 | 67,616,858 |
| FNMA Discount Notes | 01/03/12 | 0.34% | 66,020,000 | 65,904,025 |
| FNMA Discount Notes | 11/01/11 | 0.10% | 143,000,000 | 142,965,680 |
| FNMA Discount Notes | 07/15/11 | 0.13% | 50,000,000 | 49,999,500 |
| FNMA Discount Notes | 07/15/11 | 0.12% | 50,000,000 | 49,999,500 |
| IBRD Discount Note | 07/18/11 | 0.03% | 92,000,000 | 91,999,080 |
| IBRD Discount Note | 08/01/11 | 0.14% | 50,000,000 | 49,999,000 |
| IBRD Discount Note | 11/01/11 | 0.13% | 70,000,000 | 69,983,200 |
| IBRD Discount Note | 11/15/11 | 0.09% | 108,000,000 | 107,970,840 |
| US Treasury Bills | 12/29/11 | 0.10% | 200,000,000 | 199,902,000 |
| US Treasury Bills | 07/07/11 | 0.10% | 128,000,000 | 128,000,000 |
| US Treasury Bills | 08/11/11 | 0.02% | 55,000,000 | 54,998,900 |
| US Treasury Bills | 08/11/11 | 0.02% | 55,000,000 | 54,998,900 |
| US Treasury Bills | 03/08/12 | 0.26% | 100,000,000 | 99,934,000 |
| US Treasury Bills | 03/08/12 | 0.26% | 400,000,000 | 399,736,000 |
| US Treasury Bills | 09/15/11 | 0.16% | 59,000,000 | 58,997,640 |
| US Treasury Bills | 09/15/11 | 0.16% | 59,000,000 | 58,997,640 |
| US Treasury Notes | 09/30/11 | 0.05% | 50,000,000 | 50,117,000 |
| **TOTAL U.S. TREASURY AND AGENCY OBLIGATIONS** | | | **$ 4,962,731,000** | **$ 4,968,402,520** |
| | | | | |
| **CERTIFICATES OF DEPOSIT** | | | | |
| Community Bank & Trust, Ashland City | 07/29/11 | 0.30% | $ 500,000 | $ 500,000 |
| Community Bank & Trust, Ashland City | 08/15/11 | 0.30% | 2,000,000 | 2,000,000 |

*(continued)*

# STATE CASH PORTFOLIO
# AS OF JUNE 30, 2011

| Description | Maturity | Yield to Maturity | Par Value | Fair Value |
|---|---|---|---|---|
| Community Bank & Trust, Ashland City | 10/28/11 | 0.30% | $ 1,000,000 | $ 1,000,000 |
| Community Bank & Trust, Ashland City | 12/20/11 | 0.30% | 2,000,000 | 2,000,000 |
| Bank of Crockett, Bells | 07/08/11 | 0.20% | 2,000,000 | 2,000,000 |
| Bank of Crockett, Bells | 07/21/11 | 0.20% | 2,000,000 | 2,000,000 |
| Bank of Crockett, Bells | 08/11/11 | 0.20% | 2,000,000 | 2,000,000 |
| Bank of Crockett, Bells | 08/22/11 | 0.20% | 1,500,000 | 1,500,000 |
| Bank of Bradford | 10/21/11 | 0.30% | 90,000 | 90,000 |
| People's Bank and Trust Company, Byrdstown | 12/22/11 | 0.30% | 100,000 | 100,000 |
| People's Bank and Trust Company, Byrdstown | 09/06/11 | 0.30% | 200,000 | 200,000 |
| CapitalMark Bank & Trust, Chattanooga | 09/02/11 | 0.25% | 10,000,000 | 10,000,000 |
| CapitalMark Bank & Trust, Chattanooga | 09/13/11 | 0.30% | 5,000,000 | 5,000,000 |
| CapitalMark Bank & Trust, Chattanooga | 10/18/11 | 0.30% | 2,000,000 | 2,000,000 |
| Legends Bank, Clarksville | 08/12/11 | 0.20% | 1,000,000 | 1,000,000 |
| Legends Bank, Clarksville | 09/09/11 | 0.25% | 1,000,000 | 1,000,000 |
| Legends Bank, Clarksville | 09/28/11 | 0.25% | 1,000,000 | 1,000,000 |
| Landmark Community Bank, Collierville | 07/01/11 | 0.20% | 6,000,000 | 6,000,000 |
| Landmark Community Bank, Collierville | 07/01/11 | 0.20% | 5,000,000 | 5,000,000 |
| Landmark Community Bank, Collierville | 07/01/11 | 0.20% | 1,500,000 | 1,500,000 |
| Landmark Community Bank, Collierville | 07/05/11 | 0.20% | 1,000,000 | 1,000,000 |
| Landmark Community Bank, Collierville | 07/05/11 | 0.20% | 4,000,000 | 4,000,000 |
| Landmark Community Bank, Collierville | 07/05/11 | 0.20% | 5,000,000 | 5,000,000 |
| Landmark Community Bank, Collierville | 07/05/11 | 0.20% | 2,000,000 | 2,000,000 |
| Community First Bank & Trust, Columbia | 07/11/11 | 0.20% | 3,000,000 | 3,000,000 |
| Community First Bank & Trust, Columbia | 08/11/11 | 0.20% | 2,000,000 | 2,000,000 |
| Community First Bank & Trust, Columbia | 07/29/11 | 0.30% | 1,000,000 | 1,000,000 |
| Community First Bank & Trust, Columbia | 07/29/11 | 0.30% | 2,000,000 | 2,000,000 |
| Putnam 1st Mercantile Bank, Cookeville | 12/02/11 | 0.30% | 1,000,000 | 1,000,000 |
| Putnam 1st Mercantile Bank, Cookeville | 11/29/11 | 0.30% | 1,000,000 | 1,000,000 |
| Community National Bank, Dayton | 11/25/11 | 0.30% | 1,000,000 | 1,000,000 |
| Community National Bank, Dayton | 07/22/11 | 0.30% | 1,000,000 | 1,000,000 |
| Community National Bank, Dayton | 10/18/11 | 0.30% | 2,000,000 | 2,000,000 |
| The Farmers & Merchants Bank, Dyer | 11/15/11 | 0.30% | 2,000,000 | 2,000,000 |
| First Citizens National Bank, Dyersburg | 08/19/11 | 0.30% | 20,000,000 | 20,000,000 |
| First Citizens National Bank, Dyersburg | 08/19/11 | 0.30% | 3,000,000 | 3,000,000 |
| Security Bank, Dyersburg | 08/11/11 | 0.20% | 3,000,000 | 3,000,000 |
| Tennessee Commerce Bank, Franklin | 07/07/11 | 0.20% | 250,000 | 250,000 |
| Friendship Bank | 11/04/11 | 0.30% | 525,000 | 525,000 |
| Friendship Bank | 11/04/11 | 0.30% | 1,550,000 | 1,550,000 |
| Friendship Bank | 11/04/11 | 0.30% | 50,000 | 50,000 |

*(continued)*

# STATE CASH PORTFOLIO
# AS OF JUNE 30, 2011

| Description | Maturity | Yield to Maturity | Par Value | Fair Value |
|---|---|---|---|---|
| Gates Banking and Trust Company | 08/26/11 | 0.20% | $ 450,000 | $ 450,000 |
| Gates Banking and Trust Company | 08/26/11 | 0.20% | 500,000 | 500,000 |
| Gates Banking and Trust Company | 08/26/11 | 0.20% | 1,000,000 | 1,000,000 |
| Gates Banking and Trust Company | 07/08/11 | 0.20% | 350,000 | 350,000 |
| Gates Banking and Trust Company | 07/08/11 | 0.20% | 500,000 | 500,000 |
| Gates Banking and Trust Company | 07/15/11 | 0.20% | 500,000 | 500,000 |
| Gates Banking and Trust Company | 07/22/11 | 0.20% | 1,000,000 | 1,000,000 |
| Gates Banking and Trust Company | 08/12/11 | 0.20% | 1,000,000 | 1,000,000 |
| Gates Banking and Trust Company | 08/19/11 | 0.20% | 1,000,000 | 1,000,000 |
| Gates Banking and Trust Company | 07/25/11 | 0.20% | 1,300,000 | 1,300,000 |
| Gates Banking and Trust Company | 07/25/11 | 0.20% | 1,200,000 | 1,200,000 |
| Gates Banking and Trust Company | 08/08/11 | 0.20% | 250,000 | 250,000 |
| Gates Banking and Trust Company | 08/11/11 | 0.20% | 500,000 | 500,000 |
| Gates Banking and Trust Company | 08/11/11 | 0.20% | 500,000 | 500,000 |
| Bank of Gleason | 07/01/11 | 0.30% | 2,000,000 | 2,000,000 |
| Bank of Gleason | 11/04/11 | 0.30% | 350,000 | 350,000 |
| Bank of Gleason | 08/16/11 | 0.30% | 300,000 | 300,000 |
| Bank of Gleason | 10/25/11 | 0.30% | 750,000 | 750,000 |
| Bank of Halls | 07/01/11 | 0.20% | 1,000,000 | 1,000,000 |
| Bank of Halls | 08/12/11 | 0.20% | 1,600,000 | 1,600,000 |
| Bank of Halls | 07/14/11 | 0.20% | 2,700,000 | 2,700,000 |
| Clayton Bank and Trust, Henderson | 07/11/11 | 0.30% | 5,000,000 | 5,000,000 |
| Clayton Bank and Trust, Henderson | 12/13/11 | 0.30% | 5,000,000 | 5,000,000 |
| First Volunteer Bank, Jamestown | 07/22/11 | 0.30% | 500,000 | 500,000 |
| First Volunteer Bank, Jamestown | 07/22/11 | 0.30% | 200,000 | 200,000 |
| First Volunteer Bank, Jamestown | 07/22/11 | 0.30% | 500,000 | 500,000 |
| First Volunteer Bank, Jamestown | 07/22/11 | 0.30% | 450,000 | 450,000 |
| First Volunteer Bank, Jamestown | 07/22/11 | 0.30% | 300,000 | 300,000 |
| First Volunteer Bank, Jamestown | 07/22/11 | 0.30% | 500,000 | 500,000 |
| Citizens State Bank, Jasper | 07/08/11 | 0.30% | 200,000 | 200,000 |
| Citizens State Bank, Jasper | 07/26/11 | 0.30% | 200,000 | 200,000 |
| Citizens State Bank, Jasper | 07/26/11 | 0.30% | 100,000 | 100,000 |
| BB& T, Knoxville | 11/15/11 | 0.30% | 100,000,000 | 100,000,000 |
| BB& T, Knoxville | 09/23/11 | 0.40% | 100,000,000 | 100,000,000 |
| BB& T, Knoxville | 09/01/11 | 0.40% | 75,000,000 | 75,000,000 |
| The Coffee County Bank, Manchester | 08/30/11 | 0.30% | 95,000 | 95,000 |
| The Bank of Mason | 08/09/11 | 0.20% | 1,750,000 | 1,750,000 |
| The First National Bank of McMinnville | 07/22/11 | 0.20% | 9,000,000 | 9,000,000 |
| Cadence Bank, Memphis | 07/01/11 | 0.30% | 5,000,000 | 5,000,000 |

*(continued)*

# STATE CASH PORTFOLIO
# AS OF JUNE 30, 2011

| Description | Maturity | Yield to Maturity | Par Value | Fair Value |
|---|---|---|---|---|
| Cadence Bank, Memphis | 07/01/11 | 0.30% | $ 5,000,000 | $ 5,000,000 |
| Cadence Bank, Memphis | 07/01/11 | 0.30% | 5,000,000 | 5,000,000 |
| Cadence Bank, Memphis | 08/09/11 | 0.30% | 5,000,000 | 5,000,000 |
| Cadence Bank, Memphis | 07/01/11 | 0.30% | 5,000,000 | 5,000,000 |
| Independent Bank, Memphis | 07/13/11 | 0.20% | 6,000,000 | 6,000,000 |
| Patriot Bank, Millington | 07/29/11 | 0.20% | 3,000,000 | 3,000,000 |
| Patriot Bank, Millington | 08/26/11 | 0.20% | 7,000,000 | 7,000,000 |
| Civic Bank & Trust, Nashville | 09/30/11 | 0.30% | 1,000,000 | 1,000,000 |
| Fifth Third Bank, Nashville | 08/01/11 | 0.20% | 25,000,000 | 25,000,000 |
| Fifth Third Bank, Nashville | 08/01/11 | 0.20% | 25,000,000 | 25,000,000 |
| Pinnacle National Bank, Nashville | 07/15/11 | 0.20% | 20,000,000 | 20,000,000 |
| Pinnacle National Bank, Nashville | 07/06/11 | 0.20% | 5,000,000 | 5,000,000 |
| Pinnacle National Bank, Nashville | 07/06/11 | 0.20% | 15,000,000 | 15,000,000 |
| Pinnacle National Bank, Nashville | 07/06/11 | 0.20% | 25,000,000 | 25,000,000 |
| Pinnacle National Bank, Nashville | 07/06/11 | 0.20% | 30,000,000 | 30,000,000 |
| Pinnacle National Bank, Nashville | 07/25/11 | 0.20% | 35,000,000 | 35,000,000 |
| Pinnacle National Bank, Nashville | 07/25/11 | 0.20% | 40,000,000 | 40,000,000 |
| Newport Federal Bank | 12/16/11 | 0.30% | 500,000 | 500,000 |
| Newport Federal Bank | 12/16/11 | 0.30% | 500,000 | 500,000 |
| Newport Federal Bank | 08/30/11 | 0.30% | 300,000 | 300,000 |
| Newport Federal Bank | 08/30/11 | 0.30% | 95,000 | 95,000 |
| Community Trust & Banking Company, Ooltewah | 09/02/11 | 0.30% | 500,000 | 500,000 |
| Community Trust & Banking Company, Ooltewah | 11/18/11 | 0.30% | 500,000 | 500,000 |
| Community Trust & Banking Company, Ooltewah | 12/13/11 | 0.30% | 500,000 | 500,000 |
| The Hardin County Bank, Savannah | 12/16/11 | 0.30% | 1,000,000 | 1,000,000 |
| The Hardin County Bank, Savannah | 12/20/11 | 0.30% | 2,000,000 | 2,000,000 |
| Wayne County Bank, Waynesboro | 09/16/11 | 0.30% | 500,000 | 500,000 |
| Wayne County Bank, Waynesboro | 12/16/11 | 0.30% | 900,000 | 900,000 |
| **TOTAL CERTIFICATES OF DEPOSIT** | | | $ 689,105,000 | $ 689,105,000 |
| | | | | |
| **OVERNIGHT DEPOSIT ACCOUNTS** | | | | |
| Regions Bank - Overnight Deposit Account: | 07/01/11 | 0.30% | $ 950,321,858 | $ 950,321,858 |
| **TOTAL OVERNIGHT DEPOSIT ACCOUNTS** | | | $ 950,321,858 | $ 950,321,858 |

*(continued)*

# STATE CASH PORTFOLIO
# AS OF JUNE 30, 2011

| Description | Rating | Maturity | Par Value | Fair Value |
|---|---|---|---|---|
| **COMMERCIAL PAPER** | | | | |
| B A S F | A1 | 07/15/11 | $ 50,000,000 | $ 49,998,444 |
| B A S F | A1 | 07/28/11 | 50,000,000 | 49,996,250 |
| B N P | A1 | 07/01/11 | 50,000,000 | 50,000,000 |
| Cargill Global | A1 | 07/01/11 | 70,000,000 | 70,000,000 |
| Cargill Global | A1 | 07/13/11 | 30,000,000 | 29,999,100 |
| G E | A1 | 07/01/11 | 100,000,000 | 100,000,000 |
| H S B C | A1 | 07/01/11 | 50,000,000 | 50,000,000 |
| H S B C | A1 | 07/15/11 | 100,000,000 | 99,994,556 |
| Koch Industries | A1 | 07/18/11 | 25,000,000 | 24,999,056 |
| Koch Industries | A1 | 07/08/11 | 25,000,000 | 24,999,417 |
| Koch Industries | A1 | 07/15/11 | 50,000,000 | 49,997,667 |
| Pepsi | A1 | 07/22/11 | 20,000,000 | 19,998,833 |
| Pepsi | A1 | 08/08/11 | 40,000,000 | 39,996,622 |
| Toyota | A1 | 08/08/11 | 100,000,000 | 99,982,056 |
| U P S | A1 | 07/01/11 | 30,000,000 | 30,000,000 |
| U P S | A1 | 07/01/11 | 45,000,000 | 45,000,000 |
| U P S | A1 | 07/01/11 | 25,000,000 | 25,000,000 |
| **TOTAL COMMERCIAL PAPER** | | | $ 860,000,000 | $ 859,962,001 |
| **TOTAL STATE CASH PORTFOLIO** | | | **$ 7,462,157,858** | **$ 7,467,791,379** |

# BACCALAUREATE EDUCATION SYSTEM TRUST PORTFOLIO

## BACCALAUREATE EDUCATION SYSTEM TRUST
### *AS OF JUNE 30, 2011*

| **Fixed Mutual Funds** | **Units** | **Fair Value** |
|---|---|---|
| State Street Lehman Aggregate Index | 3,687,210 | $ 48,792,855 |
| **Total Fixed Mutual Funds** | | **$ 48,792,855** |

| **Equity Mutual Funds** | **Units** | **Fair Value** |
|---|---|---|
| State Street MSCI EAFE Index Fund | 1,142,279 | $ 16,784,653 |
| State Street S&P 500 Index Fund | 589,509 | 33,706,923 |
| **Total Equity Mutual Funds** | | **$ 50,491,576** |

| | |
|---|---|
| **TOTAL PORTFOLIO** | **$ 99,284,431** |

# CHAIRS OF EXCELLENCE LARGEST HOLDINGS

## LARGEST BOND HOLDINGS
### *AS OF JUNE 30, 2011*
### *BY FAIR VALUE*

| Par Value | Security Name | Yield at Market | Maturity | Moody's Quality Rating | Fair Value |
|---|---|---|---|---|---|
| $3,730,000 | US Treasury Index Linked Notes | 2.51% | 01/15/16 | Aaa | $ 4,696,529 |
| 3,250,000 | US Treasury Notes | 0.57% | 06/30/15 | Aaa | 3,326,174 |
| 3,000,000 | FHLMC Bd | 0.24% | 03/23/12 | Aaa | 3,039,375 |
| 2,870,000 | US Treasury Index Linked Bonds | 3.16% | 01/15/26 | Aaa | 3,552,718 |
| 2,517,898 | FNMA Pool #AC8040 | 3.13% | 01/01/40 | NR | 2,609,549 |
| 2,500,000 | US Treasury Infl Index Note | 2.51% | 01/15/12 | Aaa | 3,234,388 |
| 2,100,000 | US Treasury Notes | 1.13% | 03/31/17 | Aaa | 2,236,500 |
| 2,000,000 | US Treasury Bonds | 3.11% | 05/15/30 | Aaa | 2,580,624 |
| 2,000,000 | Resolution Fdg Corp Fed Book Entry Cpn | 1.55% | 04/15/17 | NR | 1,731,400 |
| 2,000,000 | Gen Elec Cap Corp Medium Term Nts | 0.75% | 06/15/12 | Aa | 2,102,892 |

*A complete portfolio listing is available upon request.*

| Mutual Funds | Units | Fair Value |
|---|---|---|
| State Street S&P 500 Index Fund | 1,509,043 | $ 86,284,041 |
| State Street MCSI EAFE Index Fund | 2,313,042 | 33,987,832 |
| **Total Mutual Funds** | | $ 120,271,873 |

Key to Ratings: All ratings presented are from Moody's Investors Service with the exception of some of the government agency securities. Moody's does not rate these securities. Standard & Poor's does provide ratings for the securities (AAA is Standard & Poor's highest rating). Government Securities are not rated per se' but are considered the best quality securities.

Moody's rates securities as follows:

| | |
|---|---|
| Aaa | Best Quality |
| Aa | High Quality |
| A | Upper Medium Quality |
| Baa | Medium Quality |
| NR | Not Rated |

The ***Pink Palace*** was originally designed to be the dream home of Clarence Saunders, a wealthy entrepreneur and founder of Piggly Wiggly groceries. The mansion got its nickname from the pink Georgian marble used in its construction.

Mr. Saunders began construction in the early 1920's. However, due to stock reversals in a fight with the New York Exchange for control of his Piggly Wiggly stock, he had to declare bankruptcy. The unfinished house was eventually given to the city of Memphis to use as a museum.

The Pink Palace Museum houses a variety of special temporary exhibits and permanent exhibits, which include natural science (geology, fossil and animal exhibits) on the first floor and cultural history on the second floor. Notable collections include the Mechanized Clyde Parke Circus, created during the Great Depression by Memphian Clyde Park and the first self-service grocery called "Piggly Wiggly".

*Photo Credit: Memphis Convention and Visitors' Bureau*


The ***Children's Museum*** creates memorable learning experiences through the joy of play in hands-on exhibits and programs.

A place where children play to learn and adults learn to play again, the museum is packed with quality informal learning experiences that are both fun and educational. Kids go on a trip down a 50-foot model of the Mississippi River, see real fish, observe live honeybee colonies and see a thunderstorm inside in WaterWORKS! They experience a flight simulator, air traffic control tower, hot air balloon, wind tunnel and real airplane cockpit in Going Places. They become "stars" on stage; paint, sculpt and draw in an art studio; weave colorful patterns on a giant loom; and sing karaoke in Art Smart. In the original museum, Cityscape, kids climb aboard a real fire engine or "drive" a sheriff's car, climb up a 22-foot tall vertical maze, shop for groceries in a kid-size market, anchor the news on CMOM-TV, dance in the disco, build a house, write a check for money, work on a car, explore a tree house, listen to an owl talk about train safety, make a tornado or earthquake and much more.

*Photo Credit: Andrea Zucker*

# BACCALAUREATE EDUCATION SYSTEM TRUST

## BACCALAUREATE EDUCATION SYSTEM TRUST

*Tennessee Code Annotated,* Title 49, Chapter 7, Part 8 sets forth the Tennessee Baccalaureate Education System Trust (BEST) Act. The Act creates a tuition program, as an agency and instrumentality of the State of Tennessee, under which parents and other interested persons may assist students in saving for tuition cost of attending colleges and universities. The tuition program is known as the BEST Program and is comprised of two types of tuition plans: The BEST Savings Plan and the BEST Prepaid College Tuition Plan.

The federal guidelines for both 529 plans are contained in Section 529 of the Internal Revenue Code. The requirements for participation and administration of the Prepaid College Tuition Plan are contained in *Chapter 1700-5-1* of the *Official Compilation of the Rules and Regulations of the State of Tennessee*.

The BEST program offers several favorable tax benefits to its participants. BEST contracts are exempt from all federal, state and local taxes if used for qualified education expenses. In addition, earnings on any distribution used to pay for qualified higher education expenses are exempt from taxation. The maximum account limit for a beneficiary in the BEST Prepaid program is $235,000.

On May 30, 2008, the BEST Savings Plan was closed in an effort to provide customers in the plan a wider range of investment options and lower fees. Effective June 1, 2008, BEST contracted with the Georgia Higher Education Savings Plan to offer the Path2College 529 Plan to Tennesseans. The contract with Georgia terminated on June 30, 2011.

## BEST PREPAID COLLEGE TUITION PLAN

The BEST Prepaid College Tuition Plan allows anyone to pay for higher education tuition in advance on behalf of a beneficiary. Tuition and mandatory fees may be purchased in increments known as tuition units. One tuition unit represents a value of one percent of the weighted average undergraduate tuition at Tennessee's four-year public universities plus an amount to cover administration and actuarial soundness of the program. The cost for one academic year of tuition at the average-priced, four-year undergraduate Tennessee public university will be covered by approximately 100 tuition units. Higher education institutions that cost more than the average Tennessee four-year public university will require more units; those that cost less will require fewer units.

Qualified expenses include tuition, fees, books, room and board, and supplies and equipment required for enrollment or attendance. The units may be used at any accredited higher education institution -- instate or out-of-state, public or private. They may also be used at vocational and technical schools or professional and graduate schools. Participants do not have to choose a specific school when they enroll in the program.

Participants may utilize BEST's website for program information, located at www.tnbest.org, to learn about the program. The site features account forms, which can be downloaded, completed, and mailed to the BEST office. Questions or comments may be e-mailed to a BEST customer service representative.

The BEST prepaid program began accepting contracts and contributions in June 1997. At June 30, 2011, BEST had 8,830 active contracts with net assets totaling $100.5 million.

On November 22, 2010, the board voted to stop selling units in the BEST Prepaid Plan. The BEST Board annually sets the weighted average tuition of Tennessee's public colleges and universities which is effective August 1 of each year. The August 1, 2011 weighted average tuition per unit payout value was $72.15.

# BACCALAUREATE EDUCATION SYSTEM TRUST

## PREPAID TUITION PLAN
## *HISTORY OF PER UNIT PAYOUT, PRICES AND FEE*

| Enrollment Fiscal Year | Unit Payout | Administrative Fee | Actuarial Soundness | Unit Price (Aug. 1-Dec. 31) | Adjustment for Purchases after December 31* | Unit Price (Jan. 1-July 31) |
|---|---|---|---|---|---|---|
| 1997 | $ 21.64 | $ 2.11 | $ - | $ 23.75 | $ - | $ 23.75 |
| 1998 | 21.64 | 2.11 | - | 23.75 | - | 23.75 |
| 1999 | 25.00 | 1.75 | - | 26.75 | 1.25 | 28.00 |
| 2000 | 27.08 | 1.92 | - | 29.00 | 1.25 | 30.25 |
| 2001 | 29.58 | 1.92 | - | 31.50 | 1.50 | 33.00 |
| 2002 | 33.51 | 0.99 | - | 34.50 | 2.35 | 36.85 |
| 2003 | 35.98 | 1.02 | - | 37.00 | 1.40 | 38.40 |
| 2004 | 40.70 | 1.30 | - | 42.00 | 1.60 | 43.60 |
| 2005 | 43.15 | 2.10 | 3.71 | 48.96 | 1.84 | 50.80 |
| 2006 | 47.71 | 2.28 | 4.07 | 54.06 | 2.03 | 56.09 |
| 2007 | 49.72 | 2.98 | 4.24 | 56.94 | 2.14 | 59.08 |
| 2008 | 53.79 | 3.13 | 4.56 | 61.48 | 2.15 | 63.63 |
| 2009 | 56.93 | 3.87 | 4.86 | 65.66 | 2.05 | 67.71 |
| 2010 | 61.20 | 3.90 | 5.22 | 70.32 | 2.20 | 72.52 |
| 2011 | 65.57 | 5.68 | 5.59 | 76.84 | - | - |
| 2012 | 72.15 | - | - | - | - | - |

*Adjustment equal to 1/2 earnings rate assumption.

On November 22, 2010, the BEST Board of Trustees voted to stop selling units in the plan.

# CAREERS NOW PROGRAM

## Careers NOW Program

College students in Tennessee have the opportunity to learn more about the operation of state government and the various career opportunities in state government through the Careers NOW Program. Students in the program work as an intern in one of the three constitutional offices for one semester. The Treasurer, the Comptroller of the Treasury, and the Secretary of State work together to match opportunities with students' interests.

Since the program's inception in 1996, over 275 students have been selected to participate. New classes begin each spring and summer semester, subject to availability or budgetary funds.

The goal of the program is to develop a pool of students who, upon graduation, will be candidates for career positions in one of the three constitutional offices. Twenty-two percent of our students have been hired into full- time positions in the three constitutional offices and throughout state government. The students receive hands on work experience and the participating institutions and constitutional offices jointly facilitate the development of a detailed curriculum to meet the academic commitment made to higher education institutions.

Careers NOW is designed to offer students a combination of practical work experience and formal training, while giving them the opportunity to see the challenges of public service. In addition to their daily work responsibilities, students attend seminars, visit state agencies, complete written work assignments, engage in opportunities to increase their overall understanding and knowledge of Tennessee state government, and research a current government issue for their special project. Past projects selected by students have included voter registration and election issues, Internet voting, prisons and capital punishment, and higher education issues.

To be eligible for the program, students must be classified as juniors, seniors, or graduate students and have a "B" average or better. Major fields of study may include Accounting, Business Administration, Computer Science, Economics, English, Finance, Geoscience, History, Journalism, Law, Library Science, Management Information Systems, Marketing, Math, Political Science, Public Administration, Public Relations, Social Science, and related fields. Previously, students have been required to be enrolled in a college or university located within Tennessee or be a resident of Tennessee but attend an out-of-state college or university.

Applicants have come from Austin Peay State University, Carson Newman College, Covenant College, Cumberland University, David Lipscomb University, East Tennessee State University, Fisk University, Maryville College, Middle Tennessee State University, Rhodes College, Tennessee State University, Tennessee Technological University, University of Memphis, University of Tennessee at Knoxville, University of Tennessee at Martin, University of the South and Vanderbilt University. The majority of the participants have been Business or Accounting majors and have come from Middle Tennessee State University, Tennessee State University and Tennessee Technological University. Approximately 40 percent of the student participants have been minorities and 38 percent of the students have come from Tennessee State University.

The Careers NOW Program accepts Tennessee residents who are attending out-of-state colleges and universities including Centre College, College of William and Mary, Furman University, Murray State, Samford University, St. Louis University, University of North Alabama and University of Washington. The expectation is that the program will benefit from a broadened base of experience and that the students will benefit from the opportunity to gain experience in state government leading to permanent employment opportunities in their home state of Tennessee.

Current program information, assignment descriptions, and program application forms are available on the Internet at www.tn.gov/treasury/now.

# CERTIFIED PUBLIC ADMINISTRATOR EDUCATIONAL INCENTIVE PAYMENT PROGRAM

## Certified Public Administrator

The University of Tennessee Institute for Public Service administers the "County Official's Certificate Training Program Act." Certain full-time county officials are eligible for an educational incentive payment if the officials have completed the continuing education requirements of the program. The UT Institute for Public Service is required to provide the Treasurer's office a listing of those officers who have successfully completed all levels of the County Officials Certificate Training Program. The educational incentive payments are issued by the State Treasurer. The State Treasurer must issue such payments no later than October 31 of each year. The program began in 1998.

For the 2010-11 fiscal year, there were 332 officials that received the $1,223 educational incentive payment. The total paid to all officials was $406,036. The following table sets out the number of payments by position.

| Officer | Number Receiving Payment |
|---|---|
| Assessor of Property | 31 |
| Circuit Court Clerk | 42 |
| Clerk & Master | 45 |
| County Clerk | 43 |
| County Mayor/County Executive | 33 |
| Criminal Court Clerk | 2 |
| General Sessions Court Clerk | 1 |
| Chief Administrative Officer of Highways | 13 |
| Juvenile Court Clerk | 4 |
| Probate Court Clerk | 1 |
| Register of Deeds | 54 |
| Sheriff | 4 |
| Trustee | 59 |
| Total | 332 |

The table below sets out a five year history of recipients to receive educational incentive payments.

| Fiscal Year Ended June 30 | Recipients | Amount Paid Per Recipient | Total Payments |
|---|---|---|---|
| 2011 | 332 | $ 1,223 | $ 406,036 |
| 2010 | 312 | 1,500 | 468,000 |
| 2009 | 287 | 1,500 | 430,500 |
| 2008 | 282 | 1,500 | 423,000 |
| 2007 | 288 | 1,500 | 432,000 |

## County Provided Incentive Payment

Each county is encouraged and authorized to provide in its annual budget for payment of an annual educational incentive to certain employees who attain the designation of a "certified public administrator" in an amount not to exceed $3,000 less any incentive payment made by the State Treasurer. Such payments shall be paid by the county by October 31 of each year. The County Mayors shall provide to the State Treasurer the amount of any educational incentive paid by the county and the number of persons receiving such incentive. Summary information is provided below:

| | |
|---|---|
| Number of counties that provided an incentive | 14 |
| Number of counties that did not provide an incentive | 43 |
| Number of counties that did not provide information | 38 |
| Total | 95 |
| Total amount of incentives paid | $235,424 |
| Total number of recipients | 198 |
| Average incentive payment | $ 1,189 |

# CHAIRS OF EXCELLENCE TRUST

## Chairs of Excellence Trust

The Chairs of Excellence (COE) Trust provides funds with which state colleges and universities are able to contract with persons of regional or national prominence to teach in specified academic areas. The program is open to all state four-year colleges and universities and the UT Space Institute.

The funding of the program is provided through contributions (corpus) made by a private donor and a matching amount by the state, thus creating a chair. A chair is authorized to spend 4% of the 3-year average market value of the chair. However, the corpus can not be spent.

Since the beginning of the program in 1984, there have been 99 chairs created, with state appropriations totaling $44 million and matching contributions totaling $55.9 million.

## Five-Year History
## *Fiscal Years 2007-2011*

| Fiscal Year | Investment Income/(Loss) | Total Spending of the Chairs | Asset Balance |
|---|---|---|---|
| 2011 | $34,346,000 | $6,561,577 | $ 243,105,645 |
| 2010 | 22,324,590 | 6,937,327 | 215,665,629 |
| 2009 | (28,334,670) | 7,441,722 | 200,843,198 |
| 2008 | (7,631,048) | 7,368,032 | 236,954,830 |
| 2007 | 33,163,435 | 6,515,606 | 252,447,384 |

## Annualized Investment Return

| | 1 Year | 5 Years | 10 Years |
|---|---|---|---|
| Domestic Equity | 30.71 % | 2.97% | 2.77% |
| International Equity | 30.34 % | 1.49% | - |
| Fixed Income | 4.70 % | 6.94% | 5.59% |
| Short-Term | 0.03 % | 2.49% | 2.40% |
| Total Portfolio | 15.68 % | 4.70% | 4.25% |

# CHAIRS OF EXCELLENCE TRUST

## Authorized Chairs of Excellence

**The University of Tennessee**

*Chattanooga*

Cline COE in Rehabilitation Technology
COE in Judaic Studies
Frierson COE in Business Leadership
Harris COE in Business
Lyndhurst COE in Arts Education
McKee COE in Learning
Miller COE in Management and Technology
Sun Trust Bank COE in the Humanities
Unum COE in Applied Mathematics
West COE in Communications and Public Affairs

*Knoxville*

Blasingame COE in Agricultural Policy Studies
Bruce COE in Marketing, Logistics and Transportation
Clayton Homes COE in Finance
COE in Science, Technology and Medical Writing
Condra COE in Computer Integrated Engineering and Manufacturing
Condra COE in Power Electronics Applications
Goodrich COE in Civil Engineering
Gore Hunger COE in Environmental Studies
Hodges COE in English
Holly COE in Political Economy
Lincoln COE in Physics
Pilot COE in Management
Racheff Chair of Material Science and Engineering
Racheff Chair of Ornamental Horticulture
Schmitt COE in History
Shumway COE in Romance Languages

*Martin*

Dunagan COE in Banking
Hendrix COE in Free Enterprise and Economics
Parker COE in Food and Fiber Industries

*Memphis*

Bronstein COE in Cardiovascular Physiology
Crippled Children's Hospital COE in Biomedical Engineering
Dunavant COE in Pediatrics
Federal Express COE in Pediatrics
First Tennessee Bank COE in Pediatrics
Gerwin COE in Physiology
Goodman COE in Medicine
Hyde COE in Rehabilitation Engineering
LeBonheur COE in Pediatrics
LeBonheur COE in Pediatrics (II)
Muirhead COE in Pathology
Plough COE in Pediatrics
Semmes-Murphey COE in Neurology
Soloway COE in Urology
UT Medical Group COE in Obstetrics and Gynecology
Van Vleet COE in Biochemistry
Van Vleet COE in Microbiology and Immunology
Van Vleet COE in Pharmacology
Van Vleet COE in Virology

*Space Institute*

Boling COE in Space Propulsion
H. H. Arnold COE in Computational Mechanics

# CHAIRS OF EXCELLENCE TRUST

## Authorized Chairs of Excellence

**Tennessee Board of Regents**

*Austin Peay State University*

- Acuff COE in Creative Arts
- Harper/James and Bourne COE in Business
- Reuther COE in Nursing
- APSU Foundation Chair of Free Enterprise

*East Tennessee State University*

- AFG Industries COE in Business and Technology
- Basler COE for Integration of Arts, Rhetoric and Sciences
- Dishner COE in Medicine
- Harris COE in Business
- Leeanne Brown and Universities Physicians Group COE in General Pediatrics
- Long Chair of Surgical Research
- Quillen COE in Teaching and Learning
- Quillen COE of Medicine in Geriatrics and Gerontology

*Middle Tennessee State University*

- Adams COE in Health Care Services
- Jones Chair of Free Enterprise
- Jones COE in Urban and Regional Planning
- Miller COE in Equine Health
- Miller COE in Equine Reproductive Physiology
- Murfree Chair of Dyslexic Studies
- National Healthcorp COE in Nursing
- Russell COE in Manufacturing Excellence
- Seigenthaler Chair of First Amendment Studies

*Tennessee State University*

- COE in Banking and Finance
- Frist COE in Business Administration

*Tennessee Technological University*

- Mayberry Chair of Business Administration
- Owen Chair of Business Administration

*University of Memphis*

- Arthur Andersen Company Alumni COE in Accounting
- Bornblum COE in Judaic Studies
- COE in Free Enterprise Management
- Feinstone COE in Molecular Biology
- Federal Express COE in Management Information Systems
- Fogelman COE in Real Estate
- Hardin COE in Combinatorics
- Hardin COE in Economics/Managerial Journalism
- Herff COE in Biomedical Engineering
- Herff COE in Computer Engineering
- Herff COE in Law
- Hoffman COE in Art History
- Lowenberg COE in Nursing
- Morris COE in International Economics
- Moss COE in English
- Moss COE in Philosophy
- Moss COE in Psychology
- Moss COE in Urban Education
- Plough COE in Audiology and Speech Language Pathology
- Sales and Marketing Executives of Memphis COE in Sales
- Sparks COE in International Relations
- Thompson Hill COE in Accounting
- Wang COE in International Business
- Wunderlich COE in Finance

# CLAIMS AGAINST THE STATE

## Claims Against The State

The primary function of the Division of Claims Administration, Board of Claims, and Tennessee Claims Commission is to provide an avenue for persons who have been damaged by the state to be heard and, if appropriate, compensated for their loss or damage. All claims are paid through the Risk Management Fund. This fund is supported by premiums paid by each state department, agency and institution. The required funding is based upon an actuarial study which reflects risk assessment and estimated losses.

The Division of Claims Administration processes claims filed against the state for the negligent operation of motor vehicles or machinery; negligent care, custody and control of persons or property; professional malpractice; workers' compensation claims by state employees; dangerous conditions on state maintained highways and bridges; and nuisances created or maintained by the state. The Division of Claims Administration also handles all employee property damage claims and tort claims. The Division of Claims Administration operates in conjunction with the Attorney General's Office and the Tennessee Claims Commission in this claims process.

The Division of Claims Administration contracts with a third party administrator for the processing of workers' compensation claims. The division's staff monitors the work done by the third party administrator and acts as a liaison between state employees and the third party administrator. For claims occurring on or after July 1, 2005, worker's compensation claim disputes are filed with the Department of Labor and Workforce Development's Benefit Review Conference program for possible resolution without litigation.

The division contracts with a managed care organization which has established a workers' compensation preferred provider network for medical treatment for injured state employees. Currently, 99.4% of all state employees have access to this network. The managed care organization also provides case management services such as pre-certification for inpatient hospital care, bill review, large case management and other services to manage the costs of workers' compensation claims. The use of a preferred provider network allows the state to negotiate further savings off workers' compensation medical bills after the mandated fee schedule reduction, which became required on January 1, 2006. Currently, the state has obtained approximately 51% savings off billed charges as a result of the fee schedule, plus an additional 3% savings (after fee schedule reduction) as a result of the preferred provider arrangement.

During fiscal year 2011, the Division of Claims Administration received 5,136 claims falling within these categories (including workers' compensation claims filed with the third party administrator). In order for a claim to be acted upon by the Division of Claims Administration, notice must be filed with the division. The division then has 90 days to make a determination on the claim. If the division is unable to act, the claim is automatically referred to the Tennessee Claims Commission. This process ensures that claims will be processed in a timely fashion.

This division also provides staff support to the Board of Claims. The Board of Claims has the authority to hear claims which do not fall within the jurisdiction of the Tennessee Claims Commission. During the 2011 fiscal year, the Board took action on one claim. The Board also reviews and approves the purchase of insurance policies by the state and makes recommendations to the Commissioner of Finance and Administration and the General Assembly regarding the required funding for the Risk Management Fund.

# CLAIMS AGAINST THE STATE

## Claims and Payment Activity
### *Fiscal Year 2011*

| Claims Activity | Payments Made |
|---|---|
| Worker's Compensation Claims | |
| Death Payments | $ 367,109 |
| Medical Payments | 14,206,183 |
| Temporary Disability | 3,794,560 |
| Permanent Disability | 8,012,299 |
| Subtotal | 26,380,151 |
| Employee Property Damage | 60,847 |
| Tort Claims | |
| Death Payments | 553,983 |
| Bodily Injury Payments | 3,278,126 |
| Property Damage Payments | 976,579 |
| Subtotal | 4,808,688 |
| **Total Claims Against the State** | **$ 31,249,686** |

## Five-Year Claims History
### *Fiscal Years 2007-2011*

| Fiscal Year | Amount of Claims Paid |
|---|---|
| 2011 | $ 31,249,686 |
| 2010 | 29,732,845 |
| 2009 | 29,502,257 |
| 2008 | 27,480,776 |
| 2007 | 25,997,535 |

## Claims Filed By Program
### *Fiscal Years 2007-2011*

| Fiscal Year | Workers' Compensation | Employee Property Damage | Tort | Total |
|---|---|---|---|---|
| 2011 | 3,296 | 132 | 1,708 | 5,136 |
| 2010 | 3,360 | 119 | 1,766 | 5,245 |
| 2009 | 3,431 | 117 | 1,289 | 4,837 |
| 2008 | 3,250 | 141 | 1,319 | 4,710 |
| 2007 | 3,579 | 115 | 1,162 | 4,856 |

# CRIMINAL INJURIES COMPENSATION FUND

## Criminal Injuries Compensation Fund

The Criminal Injuries Compensation Fund ("Fund") provides financial assistance to crime victims through two types of programs. The funding for the programs includes privilege taxes assessed in courts against criminal defendants and other offenders upon conviction, fees levied against parolees and probationers, the proceeds of bond forfeitures in felony cases and a federal grant. Jurors may also elect to donate their jury service reimbursement to the fund.

## Criminal Injuries Compensation Program

Payments made under the Criminal Injuries Compensation Program are intended to defray the costs of medical services, loss of earnings, burial costs and other pecuniary losses to either an innocent victim of a crime or to the dependents of a deceased victim. Applications for Criminal Injuries Compensation are filed with the Division of Claims Administration. During the 2011 fiscal year, 2,882 new claims were filed.

The division's staff reviews the application and obtains supporting information from the appropriate District Attorney's Office to determine eligibility for payment from the Criminal Injuries Compensation Fund. If the division cannot process a claim within 90 days, then the claim is transferred to the Tennessee Claims Commission. Eligible payments are issued promptly and are payable directly to the service provider if the bill is unpaid, to the victim for out-of-pocket expenses and, if appropriate, his or her attorney. On average, the division renders a decision on claims within 60 days.

During the 2011 fiscal year, the Division of Claims Administration made payments to victims of crime totaling $13.5 million.

Victims of drunk drivers are also paid from the Criminal Injuries Compensation Fund. When the proximate cause of a death or injury is the operator's intoxication as prohibited by T.C.A. Section 55-10-401, the victim's death or injury is eligible for compensation, not to exceed a maximum award of $30,000 plus attorney's fees.

Since the first claims were paid in 1982, the program has awarded a total of more than $228 million to crime victims.

The Division of Claims Administration has made an effort to educate members of the public of the existence and benefits of the Criminal Injuries Compensation Program by printing and distributing informative brochures explaining the program. Public awareness efforts and the use of victim assistance coordinators in each judicial district have also aided in providing the public with information about the benefits provided through the Criminal Injuries Compensation Fund.

## Sexual Assault Forensic Exam Reimbursement

In 2007, the General Assembly amended the Criminal Injuries Compensation Act to provide payment for services related to sexual assault forensic examinations. The Fund provides reimbursement to a facility that performs sexual assault forensic exams on victims of certain sexually-oriented crimes. Facilities must bill the Fund (not the victim) and cannot seek any additional payment from the victim after payment by the Fund. Payment is up to $750 for such services for crimes occurring on or after July 1, 2007. During the 2011 fiscal year, 3,023 forensic claims were filed. On average, the division renders a decision within six days.

# CRIMINAL INJURIES COMPENSATION FUND

## SOURCES OF FUNDS
## *FISCAL YEARS 2009-2011*

| Source | 2009 Amount | 2009 Percentage | 2010 Amount | 2010 Percentage | 2011 Amount | 2011 Percentage |
|---|---|---|---|---|---|---|
| Fines | $ 6,649,241 | 38% | $ 6,539,643 | 44% | $ 6,369,594 | 49% |
| Federal Funds | 5,642,000 | 32% | 5,181,000 | 34% | 3,848,000 | 29% |
| ARRA Stimulus Funds | 1,472,799 | 8% | 0 | 0% | 0 | 0% |
| Probation Fees | 2,976,080 | 17% | 2,589,475 | 17% | 2,353,382 | 18% |
| Bond Forfeitures | 698,424 | 4% | 735,349 | 5% | 464,817 | 4% |
| Other | 169,318 | 1% | 31,483 | 0% | 27,034 | 0% |
| **Total** | **$ 17,607,862** | **100%** | **$ 15,076,950** | **100%** | **$ 13,062,827** | **100%** |

## CLAIMS PAID BY CRIME OR CLAIM TYPE
## *FISCAL YEAR 2011*

| Crime or Claim Type | Number Paid | Percentage of Total Claims | Amount Paid | Percentage of Total Paid |
|---|---|---|---|---|
| Assault | 860 | 18.4% | $ 5,312,882 | 39.3% |
| Child Sexual Abuse | 374 | 8.0% | 907,649 | 6.7% |
| Homicide | 311 | 6.6% | 2,424,073 | 17.9% |
| Robbery by Force | 231 | 4.9% | 1,267,124 | 9.4% |
| Adult Sexual Assault | 199 | 4.3% | 483,051 | 3.6% |
| DUI | 49 | 1.0% | 512,369 | 3.8% |
| Hit and Run | 22 | 0.5% | 306,602 | 2.3% |
| Vehicular (non-DUI) | 8 | 0.2% | 89,548 | 0.7% |
| Arson | 5 | 0.1% | 21,116 | 0.2% |
| Kidnapping | 1 | 0.0% | 5,330 | 0.0% |
| Subtotal | 2,060 | 44.0% | $ 11,329,744 | 83.8% |
| Forensic Exam | 2,622 | 56.0% | 2,194,974 | 16.2% |
| **Grand Total** | **4,682** | **100.0%** | **$ 13,524,718** | **100.0%** |

# CRIMINAL INJURIES COMPENSATION FUND

## NEW CLAIMS FILED
## *FISCAL YEAR 2011*

| Crime or Claim Type | Number Filed |
|---|---|
| Assault | 1,214 |
| Child Sexual Abuse | 505 |
| Homicide | 419 |
| Robbery by Force | 255 |
| Adult Sexual Assault | 244 |
| DUI | 102 |
| Hit and Run | 51 |
| Vehicular (non-DUI) | 46 |
| Other | 31 |
| Child Physical Abuse | 8 |
| Kidnapping | 3 |
| Arson | 3 |
| Stalking | 1 |
| Subtotal | 2,882 |
| Forensic Exam | 3,023 |
| **Grand Total** | **5,905** |

## CLAIMS DENIED
## *FISCAL YEAR 2011*

| Criminal Injuries Claims Reason Type | Number Denied | Percentage |
|---|---|---|
| Contributory Behavior | 333 | 21.6% |
| Failure to Cooperate/Prosecute | 316 | 20.5% |
| Insufficient Documentation | 213 | 13.8% |
| Collateral Resource Covered Loss(es) | 154 | 10.0% |
| Insufficient Proof of a Crime | 81 | 5.3% |
| Ineligible Crime | 79 | 5.1% |
| Loss(es) Less than $100 | 73 | 4.7% |
| Other | 73 | 4.7% |
| Ineligible Claimant | 69 | 4.5% |
| Late Filing of Claim | 55 | 3.6% |
| Ineligible Loss(es) | 35 | 2.3% |
| Late Reporting of Crime | 33 | 2.1% |
| No Collateral Resource Information | 14 | 0.9% |
| Passenger with Drunk Driver | 11 | 0.7% |
| Claim not Notarized | 1 | 0.1% |
| **Total Denial Reasons** | **1,540** | **100.0%** |

In fiscal year 2011, 1,222 criminal injuries claims were denied. Some claims are denied for more than one reason.

# CLAIMS COMMISSION

## Claims Commission

The Claims Commission is an administrative tribunal created under Tennessee Code Annotated, Section 9-8-301, *et seq.*, to hear money damages claims against the state based on the acts or omissions of state employees in 22 statutory categories. Most notably, the Commission has jurisdiction over claims in tort (e.g. negligent care, custody and control of persons, property or animals; professional malpractice; negligent operation or maintenance of a motor vehicle; dangerous conditions on state maintained highways or state controlled real property); claims for breach of a written contract; claims for recovery of taxes paid under protest to the Department of Commerce and Insurance; state workers compensation claims and criminal injuries compensation claims. As a condition for the waiver of the state's sovereign immunity, state employees are immunized from liability for state law claims for acts or omissions within the scope of their employment, except for willful, malicious or criminal acts. Claims are payable from the Risk Management Fund.

Damages for tort claims falling within the Commission's jurisdiction are limited to $300,000 per claimant or $1,000,000 per occurrence. There is no limitation on awards for breach of contract. The maximum award for criminal injuries compensation claims is $30,000.

There are three Claims Commissioners, each of whom hears cases arising in his or her grand division. The current Commissioners are:

Nancy Miller-Herron, Western Division (Dresden)
Robert N. Hibbett, Middle Division (Nashville)
William Shults, Eastern Division (Newport)

As required by Tennessee Code Annotated, Section 9-8-302, each of the Commissioners was appointed by the Governor and confirmed by the General Assembly. In addition, the Commissioners have been residents of Tennessee for more than five years, have been residents of their respective grand divisions for more than one year, have practiced law for more than one year and do not maintain a private law practice.

The Commissioners' terms end as follows: The Eastern Division on June 30, 2017, the Middle Division on June 30, 2019 and the Western Division on June 30, 2015.

The Claims Commission has a Clerk's office in Nashville that serves all three grand divisions. The Clerk is manager and custodian of the official record of claims appealed or transferred from the Division of Claims Administration. The clerk is responsible for the management of the Commission's docket, receipt and filing of pleadings, preparation and filing of the appellate record in the cases before the Tennessee Court of Appeals and the Tennessee Supreme Court, responding to case inquiries from litigants and communicating with other state agencies on behalf of the Commission. In addition, the clerk acts as an administrative liaison between the Treasury Department and the Claims Commission.

The Claims Commission is attached to the Department of Treasury for administrative purposes. The Treasury Department processes financial and personnel transactions on behalf of the Commission. The department also provides information technology support and other administrative support to the Commission.

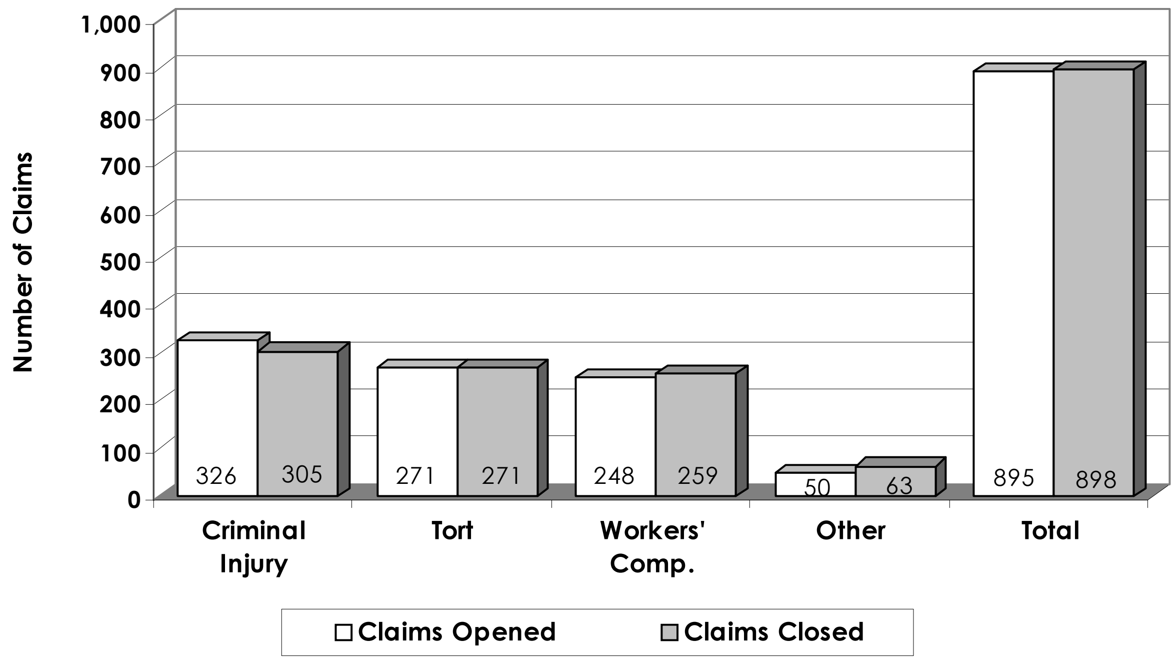
## Claims Commission's Operation

Except for claims for the recovery of taxes, which are initiated by filing with the clerk of the Claims Commission, claims are commenced by filing a notice of claim with the Division of Claims Administration or in the case of workers' compensation actions with the third party administrator. If the claim is denied, it may be appealed to the Claims Commission. Claims upon which no action is taken within 90 days automatically transfer to the Commission.

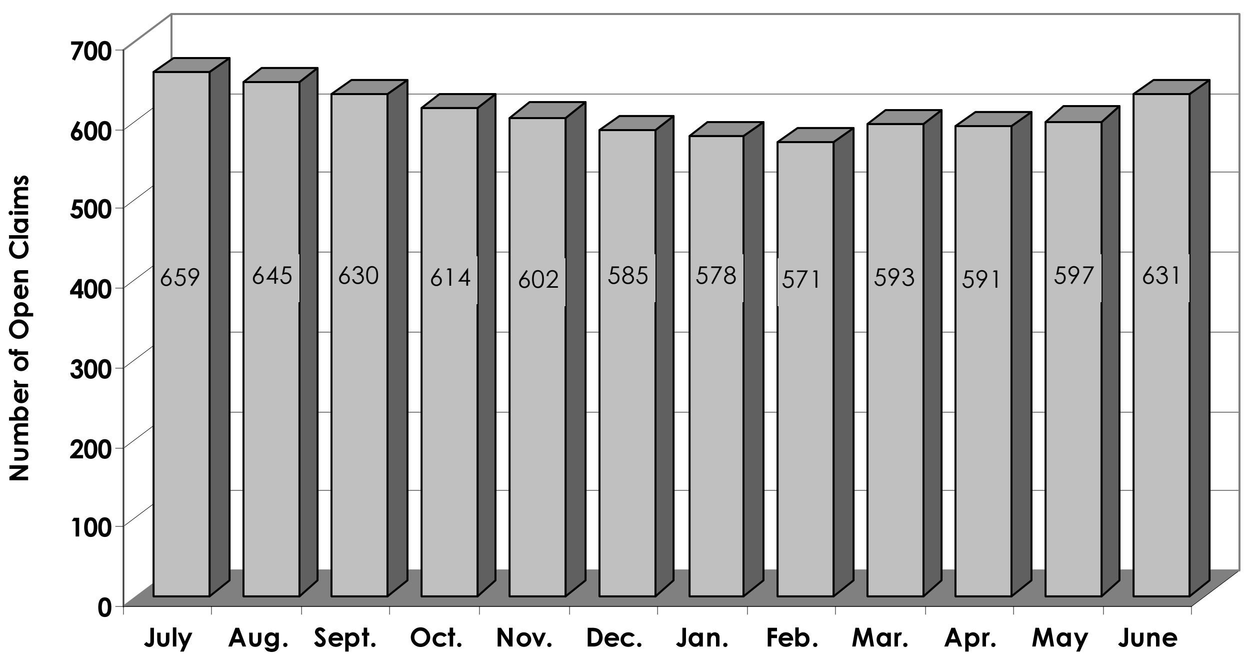
The state is represented before the Commission by the Office of the Attorney General or his delegatee. The Commission maintains two separate dockets: a regular docket consisting of claims with a monetary value of more than $25,000 and a small claims docket for claim of $25,000 and under. The Tennessee Rules of Civil Procedure are applicable. Commissioners are required to make written findings of fact and conclusions of law in all regular docket claims. At the request of two Commissioners, the Commission can sit en banc to decide any matter in which there is a disagreement among Commissioners. Decisions in regular docket claims may be appealed to the Tennessee Court of Appeals and workers' compensation cases may be appealed to the Tennessee Supreme Court. Judgments rendered against the state in the Claims Commission are paid by the Division of Claims Administration.

# CLAIMS COMMISSION

## NUMBER OF CLAIMS OPENED AND NUMBER OF DISPOSITIONS BY CLAIM TYPE
## *FISCAL YEAR 2011*




## CLAIMS COMMISSION OPEN CLAIMS
## *FISCAL YEAR 2011*



# RISK MANAGEMENT

## Division of Risk Management

The Division of Risk Management identifies and analyzes the state's exposure to property and casualty risks and implements certain risk management techniques to mitigate the state's exposure to loss. The state funds various levels of risk retention through the Risk Management Fund.

The state contracts with private insurance brokers to research the insurance marketplace and target only those insurance carriers with the highest A.M. Best ratings, which are capable and willing to provide competitive insurance quotes for the state's various lines of coverage. The lines of insurance coverage that the state acquires include property, builders' risk, aviation, fidelity and crime, boiler and machinery and fine arts. Fiscal year 2010-2011 premium costs for all lines of property and casualty coverage amounted to $4.05 million.

The state's primary level of property insurance limits was increased to $750 million. Flood coverage remained at $50 million, including properties in 100-year flood zones. Earthquake limits, once again, remained at $50 million for all zones except the New Madrid area, where limits were $25 million. The state, however, was able to purchase excess earthquake in the amount of $25 million, providing a total of $50 million coverage for New Madrid zones. The state's annual aggregate deductibles were, once again, negotiated at $5 million for property and $5 million for earthquake and flood combined. As of July 1, 2011, total insured property values were $17.8 billion.

The Builders' Risk Insurance Program provides coverage for building construction projects approved by the State Building Commission. The policy provides all-risk coverage for the state agency, general contractor and all subcontractors for the duration of the construction project. In fiscal year 2010-2011, 160 insurance certificates were issued for new construction projects approved by the State Building Commission. Certificates are renewed annually on July 1, for projects continuing from one fiscal year to the next, to ensure continuity of coverage. Coverage limits are $25 million per location and $30 million per occurrence. The contractor is responsible for providing builders' risk coverage for projects exceeding these limits. Evidence of such coverage must be provided to the state prior to beginning the construction project.

Boiler and Machinery insurance is procured to protect the state's 2,400 boiler objects. This policy performs two major functions: (1) provides boiler breakdown coverage and (2) assumes the responsibility for jurisdictional inspections on all pressure vessels. Certified inspectors evaluate all boiler objects on a scheduled basis to ensure the safe operation of the objects which, in turn, will prevent loss to human life and property. This loss prevention program has proven very effective with results showing no major incidents within the past ten years.

To protect the state from financial loss due to employee dishonesty, a fidelity and crime policy is obtained. Coverage limits are provided in the amount of $1 million per occurrence. A policy endorsement is added to extend coverage to treasurers and tax collectors.

At June 30, 2011, seven state agencies had 54 aircraft where hull insurance and liability insurance coverage quotes were obtained. The purchase of hull insurance is a business decision made by each agency for each aircraft. Liability insurance is purchased for every aircraft. The level of liability coverage varies for each aircraft and is generally based on type of aircraft, usage and size as measured by the number of seats.

In case of losses, Risk Management administers the claims process for all lines of coverage. The division coordinates the activities of the insurance carrier, independent adjusters, state facility managers and state agency contacts. For emergency situations, a restoration company is under state contract to provide immediate response to prevent costly damages. A detailed property inventory (schedule) provides the current insurable values for both buildings and contents. Agency deductibles vary according to the type of claim: (1) Property - $25,000, (2) Builders' Risk - $10,000, (3) Boiler - $10,000, (4) Fine Arts - $0 and (5) Fidelity and Crime - $100,000. If a loss exceeds the agency deductible, loss costs are paid from the Risk Management Fund until the state's annual aggregate deductibles are satisfied. Any remaining costs are the responsibility of the insurance carriers up to their policy limits.

# RISK MANAGEMENT

The prevention and control of losses are important in managing the state's risks. In FY 2010-2011, risk management staff conducted loss prevention surveys at 45 locations. A total of 147 buildings were inspected for fire/life safety hazards. During these inspections, safety violations were recorded and corrective action reports were submitted to the agencies with recommendations for safety code compliance.

## State Property
## *Summary of Key Points*
## *Fiscal Year 2010-2011*

| | | |
|---|---|---|
| Insurance Coverage Information: | | |
| Insured Property Values | $ | 17,888,235,300 |
| Primary Property Limits Per Occurrence | | 750,000,000 |
| Annual Aggregate Deductibles: | | |
| Property | $ | 5,000,000 |
| Earthquake and Flood Combined | | 5,000,000 |
| Builders' Risk | | 1,000,000 |

| | | |
|---|---|---|
| Financing of Estimated Property Losses: | | |
| Cumulative Agency Deductibles (Agency Obligation) | $ | 600,000 |
| Risk Management Fund Obligation | | 5,000,000 |
| Insurance Carrier Obligation | | 9,833,917 |
| FEMA Reimbursement (minus) | | (563,312) |
| Total Property Losses | $ | 14,870,605 |

The amount of coverage, the level of the deductibles, the selection of the insurance companies to provide coverage and the amount of the insurance premium are reviewed and approved annually by the Board of Claims.

# SMALL AND MINORITY-OWNED BUSINESS ASSISTANCE PROGRAM

## SMALL AND MINORITY-OWNED BUSINESS (SMOB) ASSISTANCE PROGRAM

Chapter 830 of the Tennessee Public Acts of 2004 created within the Treasury Department the Small and Minority-Owned Business Assistance (SMOB)Program. Chapter 830 required the Department by rule to develop an assistance program for small and minority-owned businesses, as defined in TCA 65-5-113, which will include loans, technical assistance, consulting and educational services. The legislative intent is for the Department to use the assistance provided by this program to support outreach to new, expanding and existing businesses in Tennessee that do not have reasonable access to capital markets and traditional commercial lending facilities.

The SMOB Program replaced the Small and Minority-Owned Telecommunications Business Assistance Program that was administered by the Department of Economic and Community Development. The Telecommunications Program provided loan guarantees to qualifying businesses. With all program obligations met, the program has been phased out. Whereas the Telecommunications Program focused on a specific facet of industry, the SMOB Program was designed to perpetuate growth on a less restrictive continuum.

In addition to the provision of loan proceeds and technical assistance, this program is inclusive of program services such as financial counseling, assistance with the packaging of loan proposals, developing strategies for improved cash flow management, implementing internal financial management systems, strategic planning and identifying procurement opportunities with state, federal and local government systems. Another component of the Program is the educational aspect whereby various workshops and seminars will be conducted throughout the state geared toward small and minority-owned businesses.

The principle function of the SMOB Program is to provide a significant statewide platform through a support structure that fosters the expansion of small and minority-owned businesses in Tennessee. SMOB consists of two components: loans (including lines of credit) and program services. The loans provided must be for a specific project. Acceptable purposes for loan proceeds include:

- acquisition of machinery and equipment
- working capital
- supplies and materials
- inventory
- certain other business-related activity

There are certain types of businesses that are deemed ineligible to receive assistance from the SMOB Program. Ineligible businesses include:

- churches
- non-profit organizations
- insurance companies
- real estate contractors
- real estate developers
- night clubs and any similar entertainment-oriented business
- businesses that do not create or provide jobs
- businesses not incorporated or located in Tennessee.

The infrastructure of the SMOB Program consist of a program administrative team, lenders and a service provider network. In a capsule, the Program Administrator for SMOB is Southeast Tennessee Development District who handles the daily operation of the Program by overseeing activities of the lenders who make the loans and by overseeing the activities of the service provider network who give technical assistance to the businesses that qualify for participation in the program.

Lenders for the SMOB Program are:

- Chattanooga Neighborhood Enterprises
- East Tennessee Development District
- Nashville Minority Business Development Loan Fund
- Pathway Lending
- South Central Tennessee Development District
- Tri-State Bank of Memphis

The primary service provider of technical assistance for the SMOB Program is:

- Tennessee Small Business Development Center Network

The SMOB Program was officially launched in February

## SMALL AND MINORITY-OWNED BUSINESS ASSISTANCE PROGRAM

2008 with outstanding loans at June 2011 depicted below:

| Race | Male | Female | Number of Loans | Total Loans By Race |
|---|---|---|---|---|
| African-American | $1,154,761 | $ 758,000 | 26 | $1,912,761 |
| White | 1,073,989 | 1,117,607 | 31 | 2,191,596 |
| Other | 375,000 | 125,000 | 4 | 500,000 |
| Total Loans | $2,603,750 | $2,000,607 | 61 | $4,604,357 |

Interested parties may utilize SMOB's website, located at www.tn.gov/treasury/smob, to learn about the program.

# UNCLAIMED PROPERTY DIVISION

## Unclaimed Property Division

The Treasury Department has administered the Uniform Disposition of Unclaimed Property Act since it was enacted in 1978. Administration is carried out by the Unclaimed Property Division, which operates the program in a manner designed to return unclaimed property to the rightful owner.

The Unclaimed Property Act provides that property that an organization or individual is holding for another person will be delivered to the Treasurer for custody if the holder of the property has had no contact with the owner for a period of time, normally five years, and if the holder cannot locate the owner. Once property is delivered, the Treasurer utilizes various techniques to locate the owners. There is no time limit on claiming this property.

During the period July 1, 2010 through June 30, 2011, $60.1 million of cash property was turned over to the Treasurer. This includes $5.7 million remitted by third party audit organizations from out-of-state non-reporting holders for Tennessee residents. An additional $11.4 million in proceeds from stock sales was recognized as revenue.

Entities with property to report to Tennessee's Unclaimed Property Division obtain forms, instructions, free software, and other valuable data from the Internet web site. Many entities have expressed their appreciation for this easy access to reporting tools.

The Treasurer utilizes various methods to locate owners of unclaimed property. Initially, notification to the last known address of each owner is sent. If no response is received, additional search efforts are made through Department of Labor and Workforce Development records, telephone directories, drivers' license records, external locate research tool, and other sources. Finally, the names of owners and last known addresses are advertised in newspapers throughout the state.

In addition, a searchable database of the owners' names is available on the division's Internet site: www.treasury.tn.gov/unclaim. In addition the owners' names are available on the national website Missing Money at: www.missingmoney.com. The records of unclaimed property owners are also available for viewing by the public in the Unclaimed Property office.

During the period July 1, 2010 through June 30, 2011, $23.7 million of cash property was returned by the Unclaimed Property Division to the owners or their heirs, local governments and reciprocal states.

Any local government in Tennessee that turns over unclaimed property to the state may request that the property be returned to the local government for safekeeping after it has been held by the state for 18 months. This fiscal year, $800,000 was refunded to 25 local governments.

Tennessee has reciprocal agreements with other unclaimed property programs in other states to exchange property held by one state for owners with a last known address in the other state. Tennessee received $400,000 for residents or former residents in exchange for $1.9 million paid to other states' unclaimed property offices.

Since the program began operations in 1979, $747.6 million in unclaimed property has been reported to the Treasurer and $246.2 million has been returned to owners, heirs, local governments and reciprocal states.

After all location techniques are employed, the Unclaimed Property Division is able to return approximately 60% of property that is turned over with an owner's name.

***After all location techniques are employed, the Unclaimed Property Division is able to return approximately 60% of property that is turned over with an owner's name.***

# UNCLAIMED PROPERTY DIVISION

## METHODS USED TO RETURN PROPERTY
## *FISCAL YEAR 2011*

| Location Method | Number of Accounts | Value of Claims | Average Claim Value |
|---|---|---|---|
| Website Inquiries | 11,422 | $ 9,552,775 | $ 836 |
| Staff or Other Outreach | 852 | 5,389,330 | 6,326 |
| Holder Referral or Reimbursement | 565 | 2,231,543 | 3,950 |
| Mailings to Last Known Address | 3,775 | 1,859,262 | 493 |
| Independent Locator | 27 | 1,015,872 | 37,625 |
| Advertisement and Television | 1,450 | 730,597 | 504 |
| Match with Dept. of Labor and Work Force Records | 723 | 260,130 | 360 |
| **Total Claim Payments** | 18,814 | $ 21,039,509 | $1,118 |
| Interstate Exchanges | 45 | 1,863,095 | |
| Refunds to Local Governments | 25 | 759,373 | |
| **Total Payments** | **18,884** | **$ 23,661,977** | |

## SOURCES OF UNCLAIMED PROPERTY
## *FISCAL YEARS 2007-2011*

| | 2011 | 2010 | 2009 | 2008 | 2007 |
|---|---|---|---|---|---|
| Financial Institutions | 27% | 23% | 19% | 24% | 28% |
| Corporations, Transportation, Colleges, Retailers | 23% | 26% | 27% | 26% | 22% |
| Insurance Companies | 16% | 19% | 25% | 22% | 20% |
| Securities and Brokerage Firms | 10% | 3% | 4% | 5% | 5% |
| Cities and Counties | 8% | 8% | 5% | 6% | 4% |
| Utilities | 5% | 7% | 5% | 4% | 5% |
| Hospitals and Health Care | 5% | 4% | 4% | 3% | 6% |
| Escheat and Other | 5% | 8% | 8% | 7% | 7% |
| Other States | 1% | 2% | 3% | 3% | 3% |
| **Total** | **100%** | **100%** | **100%** | **100%** | **100%** |

## ACTIVITY
## *FISCAL YEARS 2007-2011*

| | 2011 | 2010 | 2009 | 2008 | 2007 |
|---|---|---|---|---|---|
| Number of Holders Reporting | 7,577 | 6,931 | 5,999 | 5,891 | 5,531 |
| Number of Properties Received | 529,502 | 543,412 | 319,466 | 371,527 | 223,703 |
| Cash Received (not including shares sold) | $ 60,128,207 | $ 50,158,392 | $ 50,998,037 | $ 52,314,382 | $ 45,016,106 |
| Number of Shares Received | 13,412,891 | 1,859,331 | 2,224,055 | 2,257,769 | 1,364,190 |
| Value of Shares Sold | $ 11,408,829 | $ 13,659,794 | $ 9,148,704 | $ 28,157,142 | $ 6,021,856 |
| Number of Claims Paid | 18,884 | 19,446 | 21,543 | 16,982 | 15,437 |
| Cash Paid | $ 23,661,977 | $ 23,648,637 | $ 23,252,511 | $ 22,428,974 | $ 17,496,766 |
| Shares Paid | 234,684 | 254,547 | 270,135 | 223,892 | 148,952 |


The ***Lorraine Motel***, also known as the National Civil Rights Museum, in Memphis, Tennessee, is the site of the assassination of Dr. Martin Luther King, Jr. on April 4, 1968. The Lorraine Motel remained open following Dr. King's death until 1982. The Martin Luther King, Jr. Memorial Foundation purchased the property and opened the doors of the museum in 1991. The museum has hosted over 3 million visitors since opening.

Through interpretive exhibits and audio/visual displays, the museum brings to life the most significant moments of civil and human rights struggles and victories gained through the efforts and sacrifices of courageous individuals who stood by their convictions.

The National Civil Rights Museum was accredited by the American Association of Museums; only 5% of museums earn that distinction, and is one of only five U.S. accredited international sites of conscience.

*Photo Credit: National Civil Rights Museum*

The ***Fire Museum of Memphis*** is located in Fire Engine House No. 1, which was built in 1910. It features interactive and historical exhibits that teach the history of Memphis firefighting and fire safety. Major attractions include the Fire Room where you can see what it feels like to be in a burning house while learning safety practices needed to escape. Guests can step back in time and fight the flames of a burning scraper from a snorkel basket. Some fascinating exhibits include:

- The 1897 Hale Water Tower - a restored piece of firefighting apparatus used from 1897-1973 to extinguish fires in multi-level buildings.
- The Black Firefighters Exhibit - recognizes the twelve men who, in 1955, made up the first class of black fire fighters in Memphis.
- The EMS Exhibit - the actual part of an ambulance that is used to treat and transport patients to area hospitals. It is fully equipped and includes a video with related information.
- A Memorial Wall - a tribute dedicated to Memphis Firefighters who died in the line of duty.

*Photo Credit: Memphis Convention and Visitors' Bureau*

# STATUTORY DUTIES OF THE STATE TREASURER

| BOARDS AND COMMISSIONS | TENNESSEE CODE ANNOTATED SECTION |
|---|---|
| Access Improvement Project Committee | 54-2-207 |
| Advisory Board to Establish Compensation for Use of the Right-of-Way for Underground Fiber Optic Cable Facilities | 54-16-112 |
| Advisory Committee to the Trustees of the Fisk University Stieglitz Collection Art Endowment Fund | 4-20-201 |
| Advisory Council on Workers' Compensation | 50-6-121 |
| Appeals from Gift Tax Appraisals Board | 67-8-116 |
| Baccalaureate Education System Trust Board | 49-7-804 |
| Board of Claims | 9-8-101 |
| Catastrophic Injuries Fund Commission | 29-20-408 |
| Chairs of Excellence Endowment Trust | 49-7-501 |
| Collateral Pool Board | 9-4-506 |
| Commission on Crime Victims Assistance | Ex. Order 10 of 2003 |
| Commission to Purchase Surplus Federal Property | 12-1-103 |
| Council on Pensions & Insurance | 3-9-101 |
| Industrial Finance Corporation Board | 4-17-405 |
| Local Education Insurance Committee | 8-27-301 |
| Local Government Insurance Committee | 8-27-207 |
| Public Records Commission | 10-7-302 |
| Sick Leave Bank Board | 8-50-903 |
| State Board of Equalization | 4-3-5101 |
| State Building Commission | 4-15-101 |
| State Capitol Commission | 4-8-301 |
| State Funding Board | 9-9-101 |
| State Insurance Committee | 8-27-101 |
| State Trust of Tennessee | 9-4-806 |
| Tennessee Consolidated Retirement System Board of Trustees | 8-34-302 |
| Tennessee Financial Literacy Commission | 49-6-1702 |
| Tennessee Higher Education Commission | 49-7-204 |
| Tennessee Housing Development Agency | 13-23-106 |
| Tennessee Industrial Development Authority | 13-16-301 |
| Tennessee Local Development Authority | 4-31-103 |
| Tennessee Sports Hall of Fame | 4-3-5403 |
| Tennessee State School Bond Authority | 49-3-1204 |
| Tennessee Student Assistance Corporation | 49-4-202 |
| Tuition Guaranty Fund Board | 49-7-2018 |
| Workers Compensation Insurance Fund Board | 50-6-604 |

| ADMINISTRATION | TENNESSEE CODE ANNOTATED SECTION |
|---|---|
| Baccalaureate Education System Trust | 49-7-801, et seq. |
| Board of Claims | 9-8-101, et seq. |
| Chairs of Excellence Trust | 49-7-501—49-7-503 |
| Collateral Pool | 9-4-501—9-4-523 |
| Collateral Program | 9-4-101—9-4-105 |
| Council on Pensions and Insurance | 3-9-101—3-9-104 |
| Criminal Injury Compensation Fund | 29-13-101, et seq. |
| Deferred Compensation | 8-25-101, et seq.; 8-25-301, et seq. |
| Escheat | 31-6-101, et seq. |
| Flexible Benefits Plan | 8-25-501—8-25-502 |
| Investment Advisory Council | 8-37-108 |
| Investment of State Idle Cash Funds | 9-4-602 |
| Local Government Investment Pool | 9-4-704—9-4-707 |
| Old Age and Survivors Insurance Agency | 8-38-101, et seq. |
| Pooled Investment Fund | 9-4-603 |
| Receipt and Disbursement of Public Funds | 8-5-106—8-5-111; 9-4-301, et seq. |
| Small and Minority-Owned Business Assistance Program | 65-5-113 |
| State Cash Management | 9-4-106—9-4-108; 9-4-401—9-4-409 |
| State Treasurer's Office | 4-3-2401, et seq.; 8-5-101, et seq. |
| State Trust of Tennessee | 9-4-801, et seq. |
| Tennessee Claims Commission | 9-8-301, et seq. |
| Tennessee Consolidated Retirement System and Miscellaneous Systems | Title 8, Chptrs. 34, 35, 36, 37 & 39 |
| Tennessee Financial Literacy Program | 49-6-1701, et seq. |
| Unclaimed Property | 66-29-101, et seq. |
| Victims of Drunk Drivers Compensation Fund | 40-24-107 |

# EXECUTIVE STAFF DIRECTORY

| | | |
|---|---|---|
| **Treasurer's Office** | | |
| Treasurer | David H. Lillard, Jr., JD, LLM in Taxation | 615-741-2956 |
| Chief of Staff | Janice H. Cunningham | 615-741-2956 |
| Public Policy Advisor | Joy Harris | 615-532-9908 |
| Staff Assistant to the Treasurer | Joshua Stites | 615-532-9912 |
| Human Resource Director | Ann Taylor-Tharpe | 615-532-3347 |
| Director of Communications | Blake Fontenay | 615-253-2668 |
| Legislative Projects and Research Administrator | Stephanie Shackelford | 615-741-0513 |
| **Legal, Compliance and Internal Audit** | | |
| Assistant Treasurer | Christy Allen, JD | 615-253-3853 |
| General Counsel | Mary Roberts-Krause, JD | 615-253-3855 |
| Compliance Officer | Paul Robertson, JD | 615-253-4111 |
| Administrator of Old Age and Survivors Insurance | Mary Griffin, JD | 615-532-0891 |
| Administrator of Workers' Compensation Advisory Council | Lynn Ivanick, JD | 615-741-4358 |
| Interim Director of Internal Audit | Brian Derrick, CPA | 615-532-8051 |
| **Investments and Deferred Compensation** | | |
| Assistant Treasurer | Bill Abney, JD, LLM | 615-532-1167 |
| Chief Investment Officer | Michael Brakebill, CFA | 615-532-1157 |
| Deputy CIO and Fixed Income Director | Andy Palmer, CFA | 615-532-1183 |
| Senior Fixed Income Manager | Thomas Kim, CFA | 615-253-5416 |
| Equity Director | Michael Keeler, CFA | 615-532-1165 |
| Senior Equity Portfolio Manager | Jim Robinson, CFA | 615-532-1177 |
| Senior Equity Portfolio Manager | Roy Wellington, CFA | 615-532-1151 |
| Real Estate Director | Peter Katseff | 615-532-1160 |
| Director of Short-Term Investments | Tim McClure, CCM | 615-532-1166 |
| Director of Private Equity | Lamar Villere, CFA | 615-532-1154 |
| Manager of Deferred Compensation | Kaci Lantz, CFP® | 615-741-7063 |
| **Retirement Administration and Program Services** | | |
| First Deputy Treasurer | Steve Curry, CPA-inactive, CEBS, CCM | 615-532-8045 |
| TCRS Director | Jill Bachus, CPA, CGFM | 615-741-7063 |
| TCRS Assistant Director | Jamie Wayman, CPA | 615-741-7063 |
| Counseling Services Manager | Candy O'Leary | 615-741-1971 |
| Member Benefits Manager | Erica Nale | 615-741-4868 |
| Financial Services Manager | Keevia Battle, CPA | 615-741-4913 |
| Assistant Director of Concord | Fred Marshall, CPA | 615-253-4871 |
| Director of Risk Management | Steve Gregory | 615-741-1009 |
| Manager Small Minority Business Program | Jaye Chavis | 615-253-2265 |
| Director of College Savings | LaKesha Page | 615-532-5888 |
| Director of Unclaimed Property | John Gabriel | 615-253-5354 |
| Assistant Director Unclaimed Property | Kellie Williamson | 615-253-5356 |
| Director of Claims Administration | Anne Adams | 615-741-9957 |
| Criminal Injury Program Manager | Amy Dunlap | 615-741-9962 |
| East Tennessee Claims Commissioner | William O. Shults, JD | 423-623-9270 |
| Middle Tennessee Claims Commissioner | Robert Hibbett, JD | 615-253-1626 |
| West Tennessee Claims Commissioner | Nancy Miller-Herron, JD | 731-364-2440 |
| **Support Services** | | |
| Second Deputy Treasurer | Rick DuBray, CPA | 615-253-5764 |
| Director of Accounting | Kim Morrow, CPA | 615-532-3840 |
| Assistant Director of Accounting | Brian Derrick, CPA | 615-532-8051 |
| Director of Management Services | Kerry Hartley, CPA | 615-532-8552 |
| Assistant Director of Management Services | Mary Alexander | 615-253-8771 |
| Director of Information Systems | Tim Sundell | 615-532-0734 |

*The Treasurer is housed on the 1st floor of the State Capitol Building.*
*Divisions are housed on the 9th, 10th and 11th floors of the Andrew Jackson Building.*

## TREASURY STAFF

Abney, Bill
Adams, Anne
Alexander, Mary
Allen, Christy
Anderson, Sandra
Armistead, James
Arnett, Ron
Atkins, Janice[15]
Aymett, Ron[30]
Bachus, Jill[30]
Baker, Linda
Bandy, Gregory[5]
Battle, Keevia
Bauer, David
Baumgartel, Karen
Bradley, Kevin
Brakebill, Michael
Brown, Buffy
Burcham, Janet
Butler, Michelle
Butterfield, Keith
Campbell, Heath
Chandler, Joseph
Chang, Albert
Chatman, Shirley[25]
Chavis III, Jordan[5]
Christensen, Mary
Cole, Julia
Coleman, Kanika
Cook, Hope
Costa, Delcinia
Couch, Janie
Crews, Daniel
Culberson, Cavandrea
Cunningham, Janice
Curry, Steve
Curtis, Karen[5]
Curtis, Shawn
Dagnan, Derrick
Daniel, Ted
Daniels, Ruth
Darrell, Pat
Davis, Amanda
Davis, Melissa
Denney, Pam
Derrick, Brian
Dice, Darrell
Dickens, Sarah
Dills, Larissa
Dineen, Amy
Dodson, Marcus
Dorse, Bridget
Doss, Gail
DuBray, Rick
Dunlap, Amy
Elder-Baynes, Stephanie
Esaka, Cassandra[5]
Faehr, Karen
Farmer, Sharon
Farris, Carla
Fohl, Jamie
Fontenay, Blake
Fredin, Cort[10]
Fuqua, Monica[25]
Gabriel, John[15]
Gaines, Doug
Giggie, Michael
Gray, Tammy[5]
Green, Carrie
Green, Janice
Gregory, Steve[25]
Griffin, Delores
Griffin, Mary[10]
Gupta, Kushal
Hadley, Chris
Haitas, Matthew
Hall, NicoleMarie
Hall, Sherry
Hargrove, Kathy
Harris, Adrienne[5]
Harris, Joy
Hartley, Kerry[10]
Henry, Roger
Herschberg, Jennifer
Hibbett, Robert
Hicks, Brad
Hoffer, Mandy
Hudgins, Terry[5]
Hunter, Deborah[5]
Hurt, Sandra
Hyder, Patti
Ing, Jamie
Ivanick, Lynn
Jackson, Stacey
Jefferies, Brian
Jennette, Angela
Jernigan, Carla[15]
Johnson, Greg
Johnson, Roxanne[10]
Johnson, Tawana
Jones, Chris
Jorgensen, Chelsea
Katseff, Peter
Keeler, Mike
Kilpatrick, Dawn
Kim, Thomas
King, Jenny
Klar, Markus
Ladd, George
Lantz, Kaci
Li, Liren
Lillard, Jr., David
Lyon, Landon
Mackey, Wanda
Maddox, Teresa
Maloney, Brandon
Manson, Cathy
Marshall, Fred[15]
Martin, Alfredia
Mason, Justin
McBee, Johnny
McClure, Tim
McDade, Joshua[5]
McDowell, Kenneth
Mercier, Brenda
Miller-Herron, Nancy
Moore, Crystal
Morris, Blake
Morrow, Kim
Moulder, Mike
Murphy, RJ
Myers, Barbara
Myers, Rhonda[15]
Nale, Erica
Nelson, Dana
Newberry, Lori[5]
O'Leary, Candy
Oakley, Heather[5]
Oliphant, Sarah[5]
Otts, Kimberly
Oyster, David
Page, LaKesha
Palmer, Andy[5]
Parlow, Yvonne
Parton, Floyd
Patton, Janice
Payne, Jana
Picunko, Jesse[5]
Pierce, Roxanna
Pinkston, Michelle
Pirtle, Karen
Pritchett, Brad
Rand, Cheri
Redmond, William
Reynolds, Ian[5]
Rife, Faith
Roberts, Rachel
Roberts-Krause, Mary
Robertson, Paul
Robinson, Bettina
Robinson, Jim
Robinson, Mia
Rochelle, Dawn
Sabin, Stephanie
Sadler, Anthony
Sanders, Sharon[10]
Sanders, Teresa[5]
Sanford, Letha
Scott, Tammie
Sczepczenski, Heather
Shackelford, Stephanie
Shults, William
Simpson, Ben
Singleton, Lori
Smith, Anita
Smith, Danny
Smith, Robert
Smotherman, Suzanne[25]
Sprague, Andrew
Staggs, Amanda
Stembridge, Kyle
Stites, Joshua
Sundell, Tim
Swadley, Breeanna
Tahiraj, Tani
Taylor-Tharpe, Ann
Tierney, Kevin
Tucker, Anthonio
Veach, Johnny
Villere, Lamar
Wagner, Malinda[25]
Wakefield, Gayle
Wakefield, Mark
Washington, Tracey
Wayman, Jamie
Wellington, Roy
Wheeler, Gary
Whitaker, Lauren
Wilkins, Natasha
Willeby, Michael
Williams, Teresa
Williamson, Kellie[15]
Willocks, Dianne
Wilson, Martha
Wilson, Shirley
Wimmer, Genera
Wolfenbarger, Lindsey
Woodard, Vivian
Woodrum, Angela
Wright, Casey
Young, Hannah
Younglove, Sigourney[5]
Zientar, Doreen

[5] Received 5-year service award in 2011
[10] Received 10-year service award in 2011
[15] Received 15-year service award in 2011
[20] Received 20-year service award in 2011
[25] Received 25-year service award in 2011
[30] Received 30-year service award in 2011

# TREASURY INTERNET SERVICES

| | | |
|---|---|---|
| ***SERVICES TO THE PUBLIC*** | | |
| BEST | Program information, rate information, contracts, forms and newsletters | http://treasury.tn.gov/best |
| Careers NOW | Program information, calendar, campus contacts, job descriptions and applications | http://treasury.tn.gov/now/index.html |
| Claims Commission | Program information, contacts, rules and statutes | http://treasury.tn.gov/claims/index.html |
| Criminal Injury Compensation Program | Program information, forms, links to victims' programs nationwide and victims' organizations | http://treasury.tn.gov/injury/index.html |
| Small and Minority-Owned Business Program | Program information, rules and legislation | http://treasury.tn.gov/smob/index.html |
| Unclaimed Property | Search for unclaimed property, program information, links to other states' programs, holder reporting information, forms, instructions and free software | http://treasury.tn.gov/unclaim/index.html |
| ***GOVERNMENT SERVICES*** | | |
| Bank Collateral Pool | Program information, forms and participants | http://treasury.tn.gov/bank/index.html |
| Local Government Investment Pool | Information, forms, operations manual, newsletters, past rates, portfolio and investment policy | http://treasury.tn.gov/lgip/index.html |
| OASI/Social Security | Information, FICA rates, law and forms | http://treasury.tn.gov/oasi/index.html |
| ***PUBLIC EMPLOYEE BENEFIT PROGRAMS*** | | |
| Deferred Compensation | Account access, program information, benefit projection calculator and forms | http://treasury.tn.gov/dc/index.html |
| Flexible Benefits Plan | Program information and forms | http://treasury.tn.gov/flex/index.html |
| Optional Retirement Program | Program information, forms, company contacts and product information | http://treasury.tn.gov/orp/index.html |
| Risk Management | Program and claim process information, property insurance report search, safety check lists, loss control reports and employee safety | http://treasury.tn.gov/risk/index.html |
| Tennessee Consolidated Retirement System | Program information, benefits calculator, newsletters, forms, annual report, frequently asked questions and retirement planning information | http://treasury.tn.gov/tcrs/index.html |
| ***WORKERS' COMPENSATION*** | | |
| Advisory Council on Workers' Compensation | Program information, reports, video minutes/meetings and public notices | http://treasury.tn.gov/claims/wcadvisory.html |
| Workers' Compensation for State Employees Only | Program information, reporting accidents, filing claims, eligibility criteria and provider directory | http://treasury.tn.gov/wc/index.html |
| ***OTHER*** | | |
| About the Treasurer | Statutory duties and biographical information | http://treasury.tn.gov/about.html |
| Annual Report | Treasurer's Report on-line | http://treasury.tn.gov/TreasurersAnnualReport_2011.pdf |
| Tennessee Financial Literacy Commission | Program information and resolutions | http://treasury.tn.gov/FinLit/index.html |

***Germantown Painted Horses*** is a collection of life-size painted horse sculptures created by local artists. For over 60 years, it continues to be one of the more colorful and charming features of the annual Germantown Charity Horse Show.

As a promotion for the horse show and local charities, the decorative, fiberglass horses are displayed around town throughout the summer. They are auctioned off in October to raise money for area charities. Forty-five percent of the money goes to the Germantown Charity Horse Show; forty-five percent goes to the charity of the buyer's choice; and ten percent goes to the artist.

*Photo Credit: Baxter Buck*

The ***Brooks Museum of Art***, a fully private institution, was established in 1912 and opened for viewing in 1916 after Mrs. Samuel H. Brooks donated $100,000 for its construction in honor of her late husband.

Brooks' permanent collections grew as a result of generous donors such as the Kress Foundation and the Moss family. The generosity of prominent citizens, bequests, friends and support groups allows the museum to offer the highest quality exhibitions and educational programs. In 1957, the private Fine Arts Foundation was formed to allow the museum to raise money for collections and programs through the subscription of memberships. These memberships, as well as donations from private contributors, continue to fund the annual growth of the museum.

In 1965, Brooks Museum League, which helped to begin educational programs, initiated the docent program as well as the museum's first gift shop. An art reference library opened to further the museum's educational mission. In 1979, the Decorative Arts Trust was formed to gain more decorative arts and to host seminars, lectures and events to expand the appreciation and understanding of decorative arts in Memphis.

*Photo Credit: Kevin Barre Photography*

# BACCALAUREATE EDUCATION SYSTEM TRUST, EDUCATIONAL SERVICES PLAN
# INDEPENDENT AUDITOR'S REPORT

STATE OF TENNESSEE
**COMPTROLLER OF THE TREASURY**
DEPARTMENT OF AUDIT / DIVISION OF STATE AUDIT
SUITE 1500, JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-1402
PHONE (615) 401-7897 / FAX (615) 532-2765

December 19, 2011

Members of the General Assembly
and
Members of the Board of Trustees
Baccalaureate Education System Trust
and
The Honorable David H. Lillard, Jr., Treasurer
State Capitol
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying statements of fiduciary net assets of the Baccalaureate Education System Trust, Educational Services Plan, a private-purpose trust fund of the State of Tennessee, as of June 30, 2011, and June 30, 2010, and the related statements of changes in fiduciary net assets for the years then ended. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the board of the Baccalaureate Education System Trust. We do not believe that the Comptroller's service in this capacity affected our ability to conduct an independent audit of the Baccalaureate Education System Trust, Educational Services Plan.
As discussed in Note A.1., the financial statements referred to above present only the Baccalaureate Education System Trust, Educational Services Plan, a private-purpose trust fund, and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2011, and June 30, 2010, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the fiduciary net assets of the Baccalaureate Education System Trust, Educational Services Plan, of the State of Tennessee as of June 30, 2011, and June 30, 2010, and the changes in its fiduciary net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with generally accepted government auditing standards, we have also issued our report dated December 19, 2011, on our consideration of the Baccalaureate Education System Trust, Educational Services Plan's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be considered in assessing the results of our audit.

Sincerely,

Arthur A. Hayes, Jr., CPA
Director

## BACCALAUREATE EDUCATION SYSTEM TRUST, EDUCATIONAL SERVICES PLAN
## STATEMENTS OF FIDUCIARY NET ASSETS
## JUNE 30, 2011 AND JUNE 30, 2010

| | June 30, 2011 | June 30, 2010 |
|---|---|---|
| **ASSETS** | | |
| Cash and cash equivalents | $ 1,189,318 | $ 2,944,201 |
| Receivables | | |
| Investment income receivable | 810,384 | 626,196 |
| Other receivable | 60,000 | 68,812 |
| Investments, at fair value | | |
| Investment in fixed income index fund | 48,792,855 | 35,659,248 |
| Investment in equity index fund | 50,491,576 | 41,867,136 |
| **TOTAL ASSETS** | 101,344,133 | 81,165,593 |
| **LIABILITIES** | | |
| Investments purchased | 810,370 | 626,139 |
| Accounts payable | 0 | 28,086 |
| Other investment payable | 11,066 | 9,087 |
| **TOTAL LIABILITIES** | 821,436 | 663,312 |
| **NET ASSETS HELD IN TRUST FOR PLAN PARTICIPANTS** | $ 100,522,697 | $ 80,502,281 |

*See accompanying Notes to the Financial Statements.*

## BACCALAUREATE EDUCATION SYSTEM TRUST, EDUCATIONAL SERVICES PLAN
## STATEMENTS OF CHANGES IN FIDUCIARY NET ASSETS
## FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010

| | For the Year Ended June 30, 2011 | For the Year Ended June 30, 2010 |
|---|---|---|
| **ADDITIONS** | | |
| Contributions | $ 1,338,570 | $ 3,410,544 |
| Investment income | | |
| Net increase in fair value of investments | 11,945,277 | 5,944,359 |
| Interest and dividend income | 2,813,988 | 2,358,698 |
| Less: Investment expense | (42,707) | (36,423) |
| Net investment income | 14,716,558 | 8,266,634 |
| Administrative fees | 134,560 | 259,246 |
| Transfer from General Fund | 14,750,000 | 0 |
| **TOTAL ADDITIONS** | 30,939,688 | 11,936,424 |
| **DEDUCTIONS** | | |
| Refunds | 1,814,922 | 658,881 |
| Payments | 8,631,053 | 7,442,843 |
| Administrative cost | 473,297 | 388,458 |
| **TOTAL DEDUCTIONS** | 10,919,272 | 8,490,182 |
| **CHANGE IN NET ASSETS** | 20,020,416 | 3,446,242 |
| **NET ASSETS HELD IN TRUST FOR PLAN PARTICIPANTS** | | |
| **BEGINNING OF YEAR** | 80,502,281 | 77,056,039 |
| **END OF YEAR** | $ 100,522,697 | $ 80,502,281 |

*See accompanying Notes to the Financial Statements.*

# BACCALAUREATE EDUCATION SYSTEM TRUST, EDUCATIONAL SERVICES PLAN
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010

## A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. **Reporting Entity –** The Tennessee Baccalaureate Education System Trust Fund (BEST), Educational Services Plan (ESEP) is included in the State of Tennessee Financial Reporting Entity. Because of the state's fiduciary responsibility, the BEST has been included in the *Tennessee Comprehensive Annual Financial Report* as a private-purpose trust fund.

2. **Measurement Focus and Basis of Accounting –** The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

3. **Cash and Cash Equivalents –** Cash and Cash Equivalents, by definition, includes cash and short-term investments with a maturity date within three months of the acquisition date. The state's accounting policy regarding the definition of cash and cash equivalents includes cash management pools as cash. Cash received by the ESEP that cannot be invested immediately in securities, or that is needed for operations, is invested in the State Pooled Investment Fund administered by the State Treasurer or a short-term, open-end mutual fund, Northern Institutional Government Portfolio, under the contractual arrangements for master custody services.

4. **Method Used to Value Investments –** Investments are reported at fair value. Securities traded on a national exchange are valued at the last reported sales price. The fair value of investments in open-end mutual funds is based on the share price. Investment income consists of realized and unrealized appreciation (depreciation) in the fair value of investments and interest and dividend income. Interest income is recognized when earned. Securities and securities transactions are recorded in the financial statements on trade-date basis.

## B. DEPOSITS AND INVESTMENTS

In accordance with State statute, the ESEP assets may be invested in any instrument, obligation, security or property that constitutes a legal investment for assets of the Tennessee Consolidated Retirement System (TCRS). In addition, the assets of the ESEP may be pooled for investment purposes with the assets of the TCRS or any other assets under the custody of the State Treasurer. The authority for investing the assets of the ESEP is vested in its Board of Trustees and the responsibility for implementing the investment policy established by the Board is delegated to the State Treasurer. The ESEP does not maintain its own bank accounts but utilizes the State Pooled Investment Fund for its operating cash needs. The State Pooled Investment Fund is authorized by state statute to invest funds in accordance with policy guidelines approved by the Funding Board of the State of Tennessee. The current resolution of that board gives the Treasurer authority to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, certain repurchase agreements, and various U.S. Treasury and Agency obligations. The State Pooled Investment Fund (SPIF) is also authorized to enter into securities lending agreements in which U.S. Government Securities may be loaned for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities. The investment policy and required risk disclosures relative to the State Pooled Investment Fund are presented on pages 91-95 of this report.

**Credit Risk –** The ESEP does not currently own specific fixed income securities, but chooses to invest in an index fund that replicates the Barclays Aggregate Index. At June 30, 2011 and June 30, 2010, the ESEP had $48,792,855 and $35,659,248 respectively, invested in the SSgA US Aggregate Bond Index Fund.

(CONTINUED)

# BACCALAUREATE EDUCATION SYSTEM TRUST, EDUCATIONAL SERVICES PLAN NOTES TO THE FINANCIAL STATEMENTS JUNE 30, 2011 AND JUNE 30, 2010

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Credit quality ratings for the ESEP's investments in fixed income securities as of June 30, 2011 and June 30, 2010 are not available since the SSgA US Aggregate Bond Index Fund is not traded on an exchange and is unrated; however the average rating is AA for the Barclays Aggregate securities which is the basis for the SSgA US Aggregate Index at June 30, 2011 and June 30, 2010. The State Pooled Investment Fund has not obtained a credit quality rating from a nationally recognized credit ratings agency. The Northern Institutional Government Portfolio had a credit quality rating of AAA at June 30, 2011 and June 30, 2010.

The ESEP's investment policy states that the trust may acquire securities which are rated within the four highest grades at the time of acquisition by any of the recognized rating agencies. In addition, the policy requires that only the highest quality short-term debt issues, including commercial paper with ratings of A1 or P1, may be purchased. The policy further states that index funds may be utilized as an alternative to selecting individual securities.

**Interest Rate Risk –** Interest rate risk is the risk that future changes in prevailing market rates of interest will have an adverse effect on the fair value of debt investments. The fair values of securities with long terms to maturity may be highly sensitive to interest rate changes. The investment policy for the ESEP states that bonds generally will be purchased and held to maturity, but when necessary, the portfolio will be actively managed in times of volatile interest rate swings to shorten the average maturity and protect principal value. The effective duration for the SSgA US Aggregate Bond Index Fund that ESEP utilizes was 5.17 years at June 30, 2011 and 4.56 years at June 30, 2010. Duration is a measure of a debt investment's exposure to fair value changes arising from changing interest rates. It uses the present value of cash flows weighted for those cash flows as a percentage of the investment's full price.

## C. DESCRIPTION OF THE EDUCATIONAL SERVICES PLAN

The Tennessee Baccalaureate Education System Trust, Educational Services Plan, administered by the State Treasurer, was created under *Tennessee Code Annotated*, Title 49, Chapter 7, Part 8 for the purpose of improving higher education in the State of Tennessee by assisting students or their families to pay in advance, a portion of the tuition and other costs of attending colleges and universities. Under the program, a purchaser may enter into a contract with the BEST Board of Trustees to purchase tuition units on behalf of a beneficiary. Each tuition unit purchased entitles the beneficiary to an amount no greater than one percent of the weighted average tuition of Tennessee's four-year public universities during the academic term in which it is used; however, the tuition unit or equivalent funds may be used at any accredited public or private, in-state or out-of-state institution. The purchase price of the tuition unit is determined annually by the BEST Board of Trustees with the assistance of an actuary to maintain the plan's financial soundness. During the fiscal year that ended June 30, 2011, the BEST Board of Trustees voted to discontinue selling new prepaid units of tuition as of November 22, 2010 due to the rising cost of tuition. This action will have no effect on units purchased prior to this date. Refunds and tuition payments are guaranteed only to the extent that ESEP program funds are available and neither the State of Tennessee nor the BEST Board of Trustees is liable for any amount in excess of available program funds. Pursuant to provisions of *State of Tennessee Public Acts, 2010*, Public Chapter No. 1108, during the year ended June 30, 2011, the amount of $14,750,000 was transferred from the State's General Fund to the Educational Services Plan for the purpose of eliminating the current unfunded liability of the plan. The net assets held in trust for plan participants were $12,726,819 more at June 30, 2011, and $10,091,423 less at June 30, 2010, than the amounts needed to fund the outstanding tuition units at their weighted average tuition unit prices in effect at the respective dates.

# CHAIRS OF EXCELLENCE
# INDEPENDENT AUDITOR'S REPORT

STATE OF TENNESSEE
**COMPTROLLER OF THE TREASURY**
DEPARTMENT OF AUDIT / DIVISION OF STATE AUDIT
SUITE 1500, JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-1402
PHONE (615) 401-7897 / FAX (615) 532-2765

December 19, 2011

Members of the General Assembly
and
Members of the Board of Trustees
Chairs of Excellence Trust
and
The Honorable David H. Lillard, Jr., Treasurer
State Capitol
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying balance sheets of the Chairs of Excellence, a permanent fund of the State of Tennessee, as of June 30, 2011, and June 30, 2010, and the related statements of revenues, expenditures, and changes in fund balances for the years then ended. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the board of the Chairs of Excellence. We do not believe that the Comptroller's service in this capacity affected our ability to conduct an independent audit of the Chairs of Excellence.

As discussed in Note A.1., the financial statements referred to above present only the Chairs of Excellence, a permanent fund, and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2011, and June 30, 2010, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Chairs of Excellence of the State of Tennessee as of June 30, 2011, and June 30, 2010, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with generally accepted government auditing standards, we have also issued our report dated December 19, 2011, on our consideration of the Chairs of Excellence's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be considered in assessing the results of our audit.

Sincerely,

Arthur A. Hayes, Jr.

Arthur A. Hayes, Jr., CPA
Director

# CHAIRS OF EXCELLENCE BALANCE SHEETS JUNE 30, 2011 AND JUNE 30, 2010

| | June 30, 2011 | June 30, 2010 |
|---|---|---|
| **ASSETS** | | |
| Cash and cash equivalents | $ 8,154,888 | $ 10,057,548 |
| Investments, at fair value | | |
| Government securities | 80,837,836 | 75,208,612 |
| Corporate securities | 37,651,114 | 41,198,090 |
| Investment in equity mutual fund | 120,271,873 | 94,139,711 |
| Total investments | 238,760,823 | 210,546,413 |
| Receivables | | |
| Due from colleges and universities | 526,316 | 500,000 |
| Investment income receivable | 1,775,257 | 3,733,247 |
| Total receivables | 2,301,573 | 4,233,247 |
| **TOTAL ASSETS** | $249,217,284 | $224,837,208 |
| **LIABILITIES AND FUND BALANCES** | | |
| **LIABILITIES** | | |
| Due to colleges and universities | $ 1,886,589 | $ 1,839,078 |
| Due to the Academic Scholars Fund | 4,225,050 | 4,071,340 |
| Investments purchased | - | 3,261,161 |
| **TOTAL LIABILITIES** | 6,111,639 | 9,171,579 |
| **FUND BALANCES** | | |
| Nonspendable corpus | 99,929,963 | 99,929,963 |
| Restricted | 143,175,682 | 115,735,666 |
| **TOTAL FUND BALANCES** | 243,105,645 | 215,665,629 |
| **TOTAL LIABILITIES AND FUND BALANCES** | $249,217,284 | $224,837,208 |

*See accompanying Notes to the Financial Statements.*

# CHAIRS OF EXCELLENCE
## STATEMENTS OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
## FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010

| | For the Year Ended June 30, 2011 | For the Year Ended June 30, 2010 |
|---|---|---|
| **REVENUES** | | |
| Investment income | $ 34,346,000 | $ 22,324,590 |
| **TOTAL REVENUES** | 34,346,000 | 22,324,590 |
| **EXPENDITURES** | | |
| University of Tennessee | 3,429,502 | 3,534,563 |
| Tennessee Board of Regents | 3,132,075 | 3,402,764 |
| Academic Scholars Fund | 153,710 | 387,090 |
| Administrative cost | 190,697 | 177,742 |
| **TOTAL EXPENDITURES** | 6,905,984 | 7,502,159 |
| **EXCESS OF REVENUES OVER EXPENDITURES** | 27,440,016 | 14,822,431 |
| **FUND BALANCES, BEGINNING OF YEAR** | 215,665,629 | 200,843,198 |
| **FUND BALANCES, END OF YEAR** | $243,105,645 | $215,665,629 |

*See accompanying Notes to the Financial Statements.*

# CHAIRS OF EXCELLENCE
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010

## A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. **Reporting Entity –** The Chairs of Excellence (COE) Trust forms an integral part of the primary government and has been included as a permanent fund in the *Tennessee Comprehensive Annual Financial Report.*

2. **Measurement Focus and Basis of Accounting –** The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB), using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recorded when they become both measurable and available, and expenditures are recognized when the related fund liability is incurred. Interest associated with the current fiscal year is considered to be available if received in six months.

3. **Cash and Cash Equivalents –** Cash and cash equivalents by definition, includes cash and short-term investments with a maturity date within three months of the acquisition date. The state's accounting policy regarding the definition of cash and cash equivalents includes cash management pools as cash. Cash received by the COE Trust that cannot be immediately invested in securities, or that is needed for operations, is invested in either the State Pooled Investment Fund sponsored by the State of Tennessee and administered by the State Treasurer or a short-term, open-end mutual fund, Northern Institutional Government Portfolio, under the contractual arrangement for master custody services.

4. **Method Used to Value Investments –** Investments are reported at fair value. For fair value reporting, securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. The fair value of investments in open-end mutual funds is based on the share price. Investment income includes realized and unrealized appreciation (depreciation) in the fair value of investments, and interest and dividend income. Securities and securities transactions are recorded in the financial statements on trade-date basis.

5. **Fund Balances –** Nonspendable fund balance includes amounts that cannot be spent because they are legally or contractually required to be maintained intact. The COE Trust's nonspendable corpus consists of funds provided by contributions from the state, colleges and universities, and private sources. Restricted fund balance includes amounts that are restricted for specific purposes stipulated by external resource providers, constitutionally, or through enabling legislation. The COE Trust's restricted fund balance consists of investment income that must be used for funding the Chairs of Excellence program.

6. **Adoption of New Accounting Pronouncement –** During the year ended June 30, 2011, the COE Trust adopted the provisions of Statement No. 54 of the Governmental Accounting Standards Board, Fund Balance Reporting and Governmental Fund Type Definitions. The statement establishes fund balance classifications that comprise a hierarchy based primarily on the extent to which the COE Trust is bound to honor constraints on the specific purposes for which amounts can be spent. The fund balance as of June 30, 2010, has been reclassified to conform to the new pronouncement.

(*CONTINUED*)

# CHAIRS OF EXCELLENCE
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010

## B. DEPOSITS AND INVESTMENTS

State statute authorizes the funds of the COE Trust to be commingled for investment with other trust funds and other funds subject to investment by the State Treasurer. The COE Trust does not maintain its own bank accounts but utilizes the State Pooled Investment Fund for its operating cash needs. The State Pooled Investment Fund is authorized by state statute to invest funds in accordance with policy guidelines approved by the Funding Board of the State of Tennessee. The current resolution of that board gives the Treasurer authority to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, certain repurchase agreements and various U.S. Treasury and Agency obligations. The State Pooled Investment Fund is also authorized to enter into securities lending agreements in which U.S. Government Securities may be loaned for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities.

State statute also authorizes the Board of Trustees of the COE Trust to adopt an investment policy for the trust in accordance with the laws, guidelines and policies that govern investments by the Tennessee Consolidated Retirement System. The State Treasurer is responsible for the investment of trust funds in accordance with the policy established by the trustees. The investment policy of the COE Trust requires that public funds, capital gains on public funds, and all current income exceeding withdrawals be invested in fixed income securities. Private contributions may be invested in equity securities, including domestic and foreign common stocks, preferred stocks and convertible bonds. Subsequent to the initial funding of a chair, funds may be transferred from the equity corpus to the fixed income corpus but not from the fixed income corpus to the equity corpus.

(*CONTINUED*)

# CHAIRS OF EXCELLENCE
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010

As of June 30, 2011 and June 30, 2010, the COE Trust had the following investments (expressed in thousands):

| Investment Type | Fair Value as of June 30, 2011 | U.S Treasury/ Agency (1) | Credit Quality Ratings AAA | AA | A | BBB | B | CCC | Not Rated |
|---|---|---|---|---|---|---|---|---|---|
| **Debt Investments** | | | | | | | | | |
| U.S. Government Agencies | $7,386 | $1,731 | $4,615 | $1,040 | | | | | |
| U.S. Government TIPS | 25,027 | 25,027 | | | | | | | |
| U.S. Government Treasuries | 16,024 | 16,024 | | | | | | | |
| Municipal Bonds | 2,903 | | 2,381 | 522 | | | | | |
| Government Asset Backed | 1,013 | 1,013 | | | | | | | |
| Government Mortgage Backed | 28,485 | 4,152 | | | | | | | $24,333 (2) |
| Corporate Asset Backed | 929 | | 929 | | | | | | |
| Corporate Bonds | 31,033 | | 1,520 | 6,603 | $11,717 | $10,178 | | | 1,015 |
| Corporate Mortgage Backed | 5,689 | | 5,076 | | | | | $613 | |
| Total Debt Investments | $118,489 | $47,947 | $14,521 | $8,165 | $11,717 | $10,178 | $0 | $613 | $25,348 |
| **Other Investments** | | | | | | | | | |
| Commingled Funds | | | | | | | | | |
| U.S. Equity | $86,284 | | | | | | | | |
| Non - U.S. Equity | 33,988 | | | | | | | | |
| Money Market Funds (rated AAA) | 8,200 | | | | | | | | |
| Total Other Investments | $128,472 | | | | | | | | |
| Total Investments | $246,961 | | | | | | | | |
| Less: Investments Classified as Cash Equivalents on Balance Sheet | (8,200) | | | | | | | | |
| Total Investments as Shown on Balance Sheet | $238,761 | | | | | | | | |

(1) Includes obligations of the U.S. government or obligations explicitly guaranteed by the U. S. government.

(2) Includes securities that are implicitly guaranteed by the U.S. government, but are not rated by Standard and Poor's or Moody's.

| Investment Type | Fair Value as of June 30, 2010 | U.S Treasury/ Agency (1) | Credit Quality Ratings AAA | AA | A | BBB | B | CCC | Not Rated |
|---|---|---|---|---|---|---|---|---|---|
| **Debt Investments** | | | | | | | | | |
| U.S. Government Agencies | $6,319 | $1,644 | $4,675 | | | | | | |
| U.S. Government TIPS | 25,820 | 25,820 | | | | | | | |
| U.S. Government Treasuries | 16,077 | 16,077 | | | | | | | |
| Government Asset Backed | 437 | 437 | | | | | | | |
| Government Mortgage Backed | 26,555 | 4,310 | | | | | | | $22,245 (2) |
| Corporate Asset Backed | 1,236 | | 1,236 | | | | | | |
| Corporate Bonds | 28,690 | | 1,027 | $6,480 | $10,677 | $9,411 | $995 | | 100 |
| Corporate Mortgage Backed | 11,272 | | 9,390 | | | | | $1,882 | |
| Total Debt Investments | $116,406 | $48,288 | $16,328 | $6,480 | $10,677 | $9,411 | $995 | $1,882 | $22,345 |
| **Other Investments** | | | | | | | | | |
| Commingled Funds | | | | | | | | | |
| U.S. Equity | $64,994 | | | | | | | | |
| Non - U.S. Equity | 29,146 | | | | | | | | |
| Money Market Funds (rated AAA) | 10,103 | | | | | | | | |
| Total Other Investments | $104,243 | | | | | | | | |
| Total Investments | $220,649 | | | | | | | | |
| Less: Investments Classified as Cash Equivalents on Balance Sheet | (10,103) | | | | | | | | |
| Total Investments as Shown on Balance Sheet | $210,546 | | | | | | | | |

(1) Includes obligations of the U.S. government or obligations explicitly guaranteed by the U. S. government.

(2) Includes securities that are implicitly guaranteed by the U.S. government, but are not rated by Standard and Poor's or Moody's.

# CHAIRS OF EXCELLENCE
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010

**Credit Risk –** Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Credit quality ratings for the COE Trust's investments in fixed income securities as of June 30, 2011 and June 30, 2010 are included in the above schedule. Securities are rated using Standard and Poor's and/or Moody's and are presented above using the Standard and Poor's rating scale. The State Pooled Investment Fund has not obtained a credit quality rating from a nationally recognized credit ratings agency. The Northern Institutional Government Portfolio has a credit quality rating of AAA at June 30, 2011 and June 30, 2010.

The COE Trust's investment policy states that the majority of investments should be placed in high quality debt securities to produce adequate income with minimal risk. In addition, for short-term investments, the investment policy states that only the highest quality short-term debt issues should be purchased.

As noted above, the COE Trust does not maintain its own bank accounts but utilizes the State Pooled Investment Fund for its operating cash purposes. The investment policy and required risk disclosures relative to the State Pooled Investment Fund are presented on pages 91-95 of this report.

**Concentration of Credit Risk –** A concentration of investments in any one single issuer of debt securities presents a greater risk for loss in the event that the issuer fails on its obligations. The COE Trust had the following investment amounts and percentages of total investments, in organizations representing five percent or more of total investments, excluding those organizations whose issues are explicitly guaranteed by the United States government, and investments in mutual funds, external investment pools, and other pooled investments:

| | June 30, 2011 | | June 30, 2010 | |
|---|---|---|---|---|
| **Issuer Organization** | **Fair Value** | **Percentage** | **Fair Value** | **Percentage** |
| Federal National Mortgage Association | $ 20,567,915 | 8.61% | $ 19,970,283 | 9.48% |

The COE Trust's investment policy does not specifically address limitations on investing in any one issuer.

**Interest Rate Risk –** Interest rate risk is the risk that future changes in prevailing market rates of interest will have an adverse effect on the fair value of debt investments. The fair values of securities with long terms to maturity may be highly sensitive to interest rate changes. The investment policy for the COE Trust states that the maturity of its debt securities may range from short-term instruments, including investments in the State Pooled Investment Fund, to long-term bonds, with consideration of liquidity needs. However, the policy does not specifically address limits on investment maturities. The fixed income portfolio is benchmarked against the Barclays Aggregate Index and tends to have a duration within a tight range around that index. Duration is a measure of a debt investment's exposure to fair value changes arising from changing interest rates. It uses the present value of cash flows weighted for those cash flows as a percentage of the investment's full price. The COE Trust had the following investments and effective duration at June 30, 2011 and June 30, 2010 (expressed in thousands).

(*CONTINUED*)

# CHAIRS OF EXCELLENCE
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010

**Debt Investments**

*(Expressed in Thousands)*

| Investment Type | Fair Value as of June 30, 2011 | Effective Duration (years) |
|---|---|---|
| **Debt Investments** | | |
| U.S. Government Agencies | $7,386 | 2.69 |
| U.S. Government TIPS | 25,027 | 3.51 |
| U.S. Government Treasuries | 16,024 | 7.69 |
| Municipal Bonds | 2,903 | 7.60 |
| Government Asset Backed | 1,013 | 7.64 |
| Government Mortgage Backed | 28,485 | 2.17 |
| Corporate Asset Backed | 929 | 0.11 |
| Corporate Bonds | 31,033 | 5.37 |
| Corporate Mortgage Backed | 5,689 | 1.81 |
| Total Debt Investments | $118,489 | 4.22 |

| Investment Type | Fair Value as of June 30, 2010 | Effective Duration (years) |
|---|---|---|
| **Debt Investments** | | |
| U.S. Government Agencies | $ 6,319 | 3.54 |
| U.S. Government TIPS | 25,820 | 3.87 |
| U.S. Government Treasuries | 16,077 | 8.51 |
| Municipal Bonds | 0 | 0 |
| Government Asset Backed | 437 | 6.24 |
| Government Mortgage Backed | 26,555 | 1.35 |
| Corporate Asset Backed | 1,236 | 0.85 |
| Corporate Bonds | 28,690 | 5.32 |
| Corporate Mortgage Backed | 11,272 | 2.80 |
| Total Debt Investments | $116,406 | 4.15 |

**Asset Backed Securities –** The COE Trust invests in collateralized mortgage obligations (CMOs) which are mortgage backed securities. These securities are based on cash flows from interest and principal payments on underlying mortgages. Therefore, they are sensitive to prepayments by mortgagees, which may result from a decline in interest rates. The fair value of CMOs at June 30, 2011 was $5,689,161 of which $2,901,938 were CMOs that are generally more sensitive to interest rate changes. The fair value of CMOs at June 30, 2010 was $11,272,186 of which $8,075,298 were CMOs that are generally more sensitive to interest rate changes.

## C. <u>OTHER ACCOUNTING DISCLOSURES</u>

1. **Chairs of Excellence Endowment Trust –** The COE Trust is authorized by the 94th General Assembly to further the cause of education in Tennessee. The COE Trust is administered by the State Treasurer. The Trust is set up into two general accounts which equally divide any state appropriations: one for the University of Tennessee and one for the Tennessee Board of Regents. As each Chair is designated, a portion of the appropriation is transferred to a sub-account for that Chair. The awarding college or university must provide matching contributions, of which at least 50 percent of the funds are from private contributions.

   As of June 30, 2011, 99 Chairs have been established with matching contributions received totaling $55,929,963. Total contributions to the COE Trust totaled $99,929,963 as of June 30, 2011. This includes $44,000,000 from the State, $10,321,300 from Colleges and Universities, and $45,608,663 from private contributions.

2. **Academic Scholars Fund –** Funds from the Academic Scholars Fund are combined with the COE Trust for investment purposes only. The Academic Scholars Fund general account receives only the income earned on its principal and does not receive any COE Trust state contributions or appropriations. These funds are invested in domestic fixed income securities.

# CRIMINAL INJURIES COMPENSATION FUND
# INDEPENDENT AUDITOR'S REPORT

STATE OF TENNESSEE
**COMPTROLLER OF THE TREASURY**
DEPARTMENT OF AUDIT / DIVISION OF STATE AUDIT
SUITE 1500, JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-1402
PHONE (615) 401-7897 / FAX (615) 532-2765

December 19, 2011

Members of the General Assembly
and
The Honorable David H. Lillard, Jr., Treasurer
State Capitol
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying balance sheets of the Criminal Injuries Compensation Fund, a special revenue fund of the State of Tennessee, as of June 30, 2011, and June 30, 2010, and the related statements of revenues, expenditures, and changes in fund balances and revenues, expenditures, and changes in fund balances (budget and actual) for the years then ended. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note A.1., the financial statements referred to above present only the Criminal Injuries Compensation Fund, a special revenue fund, and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2011, and June 30, 2010, and the changes in its financial position and budgetary comparisons for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Criminal Injuries Compensation Fund of the State of Tennessee as of June 30, 2011, and June 30, 2010, and the changes in its financial position and budgetary comparisons for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with generally accepted government auditing standards, we have also issued our report dated December 19, 2011, on our consideration of the Criminal Injuries Compensation Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be considered in assessing the results of our audit.

Sincerely,

Arthur A. Hayes, Jr.

Arthur A. Hayes, Jr., CPA
Director

# CRIMINAL INJURIES COMPENSATION FUND
## BALANCE SHEETS
## JUNE 30, 2011 AND JUNE 30, 2010

| | June 30, 2011 | June 30, 2010 |
|---|---|---|
| **ASSETS** | | |
| Cash | $10,406,269 | $11,392,891 |
| Accounts receivable | 625,420 | 600,671 |
| Due from federal government | 3,848,000 | 5,181,000 |
| **TOTAL ASSETS** | $14,879,689 | 17,174,562 |
| **LIABILITIES AND FUND BALANCES** | | |
| **LIABILITIES** | | |
| Accounts payable | $ 113,574 | 135,178 |
| Claims liability | 5,620,078 | 6,342,467 |
| **TOTAL LIABILITIES** | 5,733,652 | 6,477,645 |
| **FUND BALANCES** | | |
| Committed for victims of drunk drivers (see Note B.2) | 1,283,944 | 1,537,108 |
| Committed for compensation under the Criminal Injuries Compensation Act | 7,862,093 | 9,159,809 |
| **TOTAL FUND BALANCES** | 9,146,037 | 10,696,917 |
| **TOTAL LIABILITIES AND FUND BALANCES** | $14,879,689 | $17,174,562 |

*See accompanying Notes to the Financial Statements.*

# CRIMINAL INJURIES COMPENSATION FUND
## STATEMENTS OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
## FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010

| | For the Year Ended June 30, 2011 | For the Year Ended June 30, 2010 |
|---|---|---|
| **REVENUES** | | |
| State | | |
| Fines | $ 6,369,594 | $ 6,539,643 |
| Fees | 2,353,382 | 2,589,475 |
| Federal | 3,848,000 | 5,181,000 |
| Interest income | 19,749 | 27,320 |
| Other | 472,102 | 739,512 |
| **TOTAL REVENUES** | 13,062,827 | 15,076,950 |
| **EXPENDITURES** | | |
| Claim payments | 13,200,484 | 12,819,851 |
| Victims' coalition grant | 100,000 | 100,000 |
| District Attorneys General grant | 230,400 | 223,140 |
| Administrative cost | 1,082,823 | 911,691 |
| **TOTAL EXPENDITURES** | 14,613,707 | 14,054,682 |
| **EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES** | (1,550,880) | 1,022,268 |
| **FUND BALANCES, BEGINNING OF YEAR** | 10,696,917 | 9,674,649 |
| **FUND BALANCES, END OF YEAR** | $ 9,146,037 | $10,696,917 |

*See accompanying Notes to the Financial Statements.*

# CRIMINAL INJURIES COMPENSATION FUND
## STATEMENTS OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
### BUDGET AND ACTUAL (BUDGETARY BASIS) FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010

| | For the Year Ended June 30, 2011 | | | For the Year Ended June 30, 2010 | | |
|---|---|---|---|---|---|---|
| | Original Budget | Final Budget | Actual (Budgetary Basis) | Original Budget | Final Budget | Actual (Budgetary Basis) |
| **SOURCES OF FINANCIAL RESOURCES** | | | | | | |
| **FUND BALANCES, BEGINNING OF YEAR** | $ 10,696,917 | $ 10,696,917 | $ 10,696,917 | $ 9,674,649 | $ 9,674,649 | $ 9,674,649 |
| **REVENUES** | | | | | | |
| Fines | 6,600,000 | 6,600,000 | 6,369,594 | 4,710,000 | 4,710,000 | 6,539,643 |
| Fees | 3,000,000 | 3,000,000 | 2,353,382 | 2,967,000 | 2,967,000 | 2,589,475 |
| Federal | 3,700,000 | 3,700,000 | 3,848,000 | 5,025,000 | 5,025,000 | 5,181,000 |
| Interest income | 0 | 0 | 19,749 | 0 | 0 | 27,320 |
| Other | 900,000 | 900,000 | 472,102 | 550,000 | 550,000 | 739,512 |
| **TOTAL SOURCES OF FINANCIAL RESOURCES** | 24,896,917 | 24,896,917 | 23,759,744 | 22,926,649 | 22,926,649 | 24,751,599 |
| **USES OF FINANCIAL RESOURCES** | | | | | | |
| **EXPENDITURES** | | | | | | |
| Claim payments | 15,000,000 | 14,676,860 | 13,200,484 | 15,030,000 | 14,706,860 | 12,819,851 |
| Victims' coalition grant | 0 | 100,000 | 100,000 | 0 | 100,000 | 100,000 |
| District Attorneys General grant | 0 | 223,140 | 230,400 | 0 | 223,140 | 223,140 |
| Administrative cost | 900,000 | 900,000 | 1,082,823 | 850,000 | 850,000 | 911,691 |
| **TOTAL USES OF FINANCIAL RESOURCES** | 15,900,000 | 15,900,000 | 14,613,707 | 15,880,000 | 15,880,000 | 14,054,682 |
| **FUND BALANCES, END OF YEAR** | $ 8,996,917 | $ 8,996,917 | $ 9,146,037 | $ 7,046,649 | $ 7,046,649 | $ 10,696,917 |

*See accompanying Notes to the Financial Statements.*

# CRIMINAL INJURIES COMPENSATION FUND
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010

## A. Summary of Significant Accounting Policies

1. **Reporting Entity –** The Criminal Injuries Compensation Fund (CICF) is part of the primary government and has been included in the *Tennessee Comprehensive Annual Financial Report* as a special revenue fund. The Criminal Injuries Compensation Program is funded through fines assessed in courts against certain criminal defendants upon conviction, fees levied against parolees and probationers, proceeds from bond forfeitures in felony cases, donations from individuals serving as jurors, interest income and a federal grant. Payments made under the CIC program are intended to defray the costs of medical services, loss of earnings, burial costs, and other pecuniary losses to either the victim of a crime or to the dependents of deceased victims.

2. **Measurement Focus and Basis of Accounting –** The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB) using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recorded when they become both measurable and available, and expenditures are recognized at the time the fund liabilities are incurred. For revenue recognition purposes, fines and bond forfeitures are considered to be available if received in the first sixty days of the new fiscal year. Federal grants, departmental services, and interest associated with the current fiscal year are all considered to be available if received in six months. All other revenue items are considered to be measurable and available only when cash is received by the Criminal Injuries Compensation Fund.

   Generally, the CICF receives both restricted and committed resources. Restricted funds are those that are restricted for specific purposes stipulated by external resource providers, constitutionally, or through enabling legislation. Committed funds can only be used for specific purposes as a result of constraints imposed by the Tennessee General Assembly-the fund's highest level of decision-making authority. Committed amounts cannot be used for any other purpose unless the Tennessee General Assembly removes those constraints by the taking the same type of action (i.e., legislation). When both the restricted and other fund balalnce resources are available for use, it is the policy for the fund to use the restricted resources first, followed by the committed amounts.

3. **Cash –** The Criminal Injuries Compensation Fund does not maintain its own bank accounts but utilizes the State Pooled Investment Fund for its operating cash needs. The State Pooled Investment Fund is authorized by state statute to invest funds in accordance with policy guidelines approved by the Funding Board of the State of Tennessee. The current resolution of that board gives the Treasurer authority to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, certain repurchase agreements, and various U.S. Treasury and Agency obligations. The State Pooled Investment Fund is also authorized to enter into securities lending agreements in which U.S. Government Securities may be loaned for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities. The State Pooled Investment Fund is not rated by a nationally recognized statistical ratings agency. The investment policy and required risk disclosures relative to the State Pooled Investment Fund are presented on pages 91-95 of this report.

4. **Budgetary Process –** Legislation requires that annual budgets be adopted for special revenue funds. The CICF budget is included in the budget presented by the Governor to the General Assembly at the beginning of each annual legislative session. The CICF annual budget is prepared on the modified accrual basis of accounting. Budgetary control is maintained at the departmental level. Budget revisions during the year, reflecting program changes or administrative intradepartmental transfers, may be affected with certain executive and legislative branch approval. Only the legislature may transfer appropriations between departments.

# CRIMINAL INJURIES COMPENSATION FUND
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010

5. **Adoption of New Accounting Pronouncement –** During the year ended June 30, 2011, the fund adopted the provisions of Statement No. 54 of the Governmental Accounting Standards Board, *Fund Balance Reporting and Governmental Fund Type Definitions.* The statement establishes fund balance classifications that comprise a hierarchy based primarily on the extent to which the fund is bound to honor constraints on the specific purposes for which amounts in the fund can be spent. The fund balance as of June 30, 2010 has been reclassified to conform to the new pronouncement.

## B. Other Accounting Disclosures

1. **Due from Federal Government –** The receivable shown on the Balance Sheets as due from federal government includes funds for a grant awarded to the CICF under the Victims of Crime Act Formula Grant Program by the Department of Justice, Office of Justice Programs.

2. **Committed Fund Balance –** A portion of the fund balance has been committed for the Victims of Drunk Drivers Compensation Fund (VDDC) which is included in the Criminal Injuries Compensation Fund. A requirement of the CICF and VDDC combination is that a reserve be established annually for an amount equal to three times the awards paid for VDDC during the fiscal year. *Chapter 761 of the Public Acts of 1992* discusses the fund combination as well as the VDDC reserve requirement.

# FLEXIBLE BENEFITS PLAN
# INDEPENDENT AUDITOR'S REPORT

STATE OF TENNESSEE
**COMPTROLLER OF THE TREASURY**
DEPARTMENT OF AUDIT / DIVISION OF STATE AUDIT
SUITE 1500, JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-1402
PHONE (615) 401-7897 / FAX (615) 532-2765

December 19, 2011

Members of the General Assembly
and
The Honorable David H. Lillard, Jr., Treasurer
State Capitol
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying statements of fiduciary net assets of the Flexible Benefits Plan, an employee benefit trust fund of the State of Tennessee, as of June 30, 2011, and June 30, 2010, and the related statements of changes in fiduciary net assets for the years then ended. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note A.1., the financial statements referred to above present only the Flexible Benefits Plan, an employee benefit trust fund, and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2011, and June 30, 2010, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the fiduciary net assets of the Flexible Benefits Plan of the State of Tennessee as of June 30, 2011, and June 30, 2010, and the changes in its fiduciary net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with generally accepted government auditing standards, we have also issued our report dated December 19, 2011, on our consideration of the Flexible Benefits Plan's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be considered in assessing the results of our audit.

Sincerely,

Arthur A. Hayes, Jr.

Arthur A. Hayes, Jr., CPA
Director

## FLEXIBLE BENEFITS PLAN
## STATEMENTS OF FIDUCIARY NET ASSETS
## JUNE 30, 2011 AND JUNE 30, 2010

| | June 30, 2011 | June 30, 2010 |
|---|---|---|
| **ASSETS** | | |
| Cash | $1,225,992 | $ 751,250 |
| Contributions receivable | 301,421 | 298,189 |
| **TOTAL ASSETS** | 1,527,413 | 1,049,439 |
| **LIABILITIES** | | |
| Accounts payable | 52,066 | 842 |
| **TOTAL LIABILITIES** | 52,066 | 842 |
| **NET ASSETS** | | |
| Held in trust for employees' flexible benefits | $1,475,347 | $1,048,597 |

*See accompanying Notes to the Financial Statements.*

## FLEXIBLE BENEFITS PLAN
## STATEMENTS OF CHANGES IN FIDUCIARY NET ASSETS
## FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010

| | June 30, 2011 | June 30, 2010 |
|---|---|---|
| **ADDITIONS** | | |
| Employee contributions | $8,555,379 | $ 8,725,267 |
| **TOTAL ADDITIONS** | 8,555,379 | 8,725,267 |
| **DEDUCTIONS** | | |
| Employee reimbursements | 7,964,291 | 8,516,979 |
| Administrative cost | 164,338 | 143,516 |
| **TOTAL DEDUCTIONS** | 8,128,629 | 8,660,495 |
| **CHANGE IN NET ASSETS** | 426,750 | 64,772 |
| **NET ASSETS, BEGINNING OF YEAR** | 1,048,597 | 983,825 |
| **NET ASSETS, END OF YEAR** | $1,475,347 | $ 1,048,597 |

*See accompanying Notes to the Financial Statements.*

# FLEXIBLE BENEFITS PLAN
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010

## A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. **Reporting Entity –** The Flexible Benefits Plan is made available to state employees as an employee benefit. This plan is included in the State of Tennessee Financial Reporting Entity. Because of the state's fiduciary responsibility, the Flexible Benefits Plan is included in the *Tennessee Comprehensive Annual Financial Report (CAFR)* as an employee benefit trust fund. The state offers its employees a cafeteria plan created in accordance with *Internal Revenue Code Section 125*. The plan is available on an optional basis to all state employees. Through the plan, employees may elect to direct a portion of their salary to pay for certain benefits. Benefits which may be purchased through the plan include state group medical insurance, state group dental insurance, out-of-pocket medical expenses and/or dependent care expenses. Because elections must be filed before the salary or the benefits are received and because salary directed to the plan may not be withdrawn by participants for any other purpose, salary directed to the plan is exempt from federal income tax and social security tax. Elections made by employees may not be changed during the calendar plan year except in the event of a corresponding change in the participant's family status. Participants may claim expenses incurred through March 15th following the end of the plan year. Any contributions to the plan not withdrawn are forfeited to the state and are used for defraying administrative costs. In calendar year 2009, the state added reimbursement accounts for transportation and parking expenses in accordance with *Internal Revenue Code Section 132*. These plans operate in much the same manner as the *Section 125* plans in that employees may elect to direct a portion of their salary tax-exempt to pay for transportation or parking expenses. However, there are no restrictions on time of enrollment or account changes and any contributions not used will be rolled forward to the following year instead of forfeited.

2. **Measurement Focus and Basis of Accounting –** The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded at the time liabilities are incurred.

3. **Cash –** The Flexible Benefits Plan does not maintain its own bank accounts but utilizes the State Pooled Investment Fund for its operating cash needs. The State Pooled Investment Fund is authorized by state statute to invest funds in accordance with policy guidelines approved by the Funding Board of the State of Tennessee. The current resolution of that board gives the Treasurer authority to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, certain repurchase agreements, and various U.S. Treasury and Agency obligations. The State Pooled Investment Fund is also authorized to enter into securities lending agreements in which U.S. Government Securities may be loaned for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities. The State Pooled Investment Fund is not rated by a nationally recognized statistical ratings agency. The investment policy and required risk disclosures relative to the State Pooled Investment Fund are presented on pages 91-95 of this report.

4. **Participant Contribution Forfeitures and Plan Administration –** Participant contributions not reimbursed to participants and forfeited to the plan for the latest closed plan year are transferred to the Treasury Department and applied toward funding a portion of the plan administrative cost. The remaining administrative costs for the plan are recovered directly from funds of the participating employer agencies. The amount forfeited is reflected on the Statement of Changes in Fiduciary Net Assets as administrative cost.

# RISK MANAGEMENT FUND
# INDEPENDENT AUDITOR'S REPORT

STATE OF TENNESSEE
**COMPTROLLER OF THE TREASURY**
DEPARTMENT OF AUDIT / DIVISION OF STATE AUDIT
SUITE 1500, JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-1402
PHONE (615) 401-7897 / FAX (615) 532-2765

December 19, 2011

Members of the General Assembly
and
Members of the Board of Claims
and
The Honorable David H. Lillard, Jr., Treasurer
State Capitol
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying statements of net assets of the Risk Management Fund, an internal service fund of the State of Tennessee, as of June 30, 2011, and June 30, 2010, and the related statements of revenues, expenses, and changes in fund net assets and cash flows for the years then ended. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the Board of Claims. We do not believe that the Comptroller's service in this capacity affected our ability to conduct an independent audit of the Risk Management Fund.

As discussed in Note A.1., the financial statements referred to above present only the Risk Management Fund, an internal service fund, and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2011, and June 30, 2010, and the changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Risk Management Fund of the State of Tennessee as of June 30, 2011, and June 30, 2010, and the changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with generally accepted government auditing standards, we have also issued our report dated December 19, 2011, on our consideration of the Risk Management Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be considered in assessing the results of our audit.

Sincerely,

Arthur A. Hayes, Jr., CPA
Director

# RISK MANAGEMENT FUND
# STATEMENTS OF NET ASSETS
# JUNE 30, 2011 AND JUNE 30, 2010

| | June 30, 2011 | June 30, 2010 |
|---|---|---|
| **ASSETS** | | |
| Current assets | | |
| Cash | $ 107,638,216 | $ 114,501,418 |
| Accounts receivable | 86,600 | 0 |
| Total current assets | 107,724,816 | 114,501,418 |
| Noncurrent assets | | |
| Due from federal government | 10,372,508 | 8,998,081 |
| **TOTAL ASSETS** | 118,097,324 | 123,499,499 |
| **LIABILITIES** | | |
| Current liabilities | | |
| Accounts payable | 888,870 | 573,973 |
| Deferred revenue | 8,000 | 8,000 |
| Claims liability | 44,753,322 | 35,226,021 |
| Total current liabilities | 45,650,192 | 35,807,994 |
| Noncurrent liabilities | | |
| Claims liability | 58,974,305 | 71,403,765 |
| **TOTAL LIABILITIES** | 104,624,497 | 107,211,759 |
| **NET ASSETS - UNRESTRICTED** | $ 13,472,827 | $ 16,287,740 |

*See accompanying Notes to the Financial Statements.*

## RISK MANAGEMENT FUND
## STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
## FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010

| | For the Year Ended June 30, 2011 | For the Year Ended June 30, 2010 |
|---|---|---|
| **OPERATING REVENUES** | | |
| Casualty premiums | $ 41,045,900 | $ 20,976,300 |
| Property premiums | 6,735,700 | 6,142,500 |
| **TOTAL OPERATING REVENUES** | 47,781,600 | 27,118,800 |
| **OPERATING EXPENSES** | | |
| Torts | | |
| Death | 553,983 | 1,341,010 |
| Bodily injury | 3,278,126 | 3,988,802 |
| Property damage | 976,579 | 834,951 |
| Total Torts | 4,808,688 | 6,164,763 |
| Workers' Compensation | | |
| Death | 367,109 | 147,503 |
| Medical | 14,206,183 | 11,706,953 |
| Temporary disability | 3,794,560 | 3,123,938 |
| Permanent disability | 8,012,299 | 8,560,608 |
| Total Workers' Compensation | 26,380,151 | 23,539,002 |
| Property Damage | | |
| Employee property | 60,847 | 29,080 |
| State owned property | 12,517,066 | 2,879,031 |
| Total Property Damage | 12,577,913 | 2,908,111 |
| Property insurance premiums | 3,910,151 | 3,370,810 |
| Professional/Administrative | 9,354,811 | 8,915,287 |
| Addition to (reduction of) accrued liability | (4,838,772) | 8,473,946 |
| **TOTAL OPERATING EXPENSES** | 52,192,942 | 53,371,919 |
| **OPERATING LOSS** | (4,411,342) | (26,253,119) |
| **NON-OPERATING REVENUES** | | |
| Grant revenue | 1,374,426 | 5,850,000 |
| Interest income | 219,778 | 396,266 |
| Taxes | 2,225 | 2,200 |
| **TOTAL NON-OPERATING REVENUES** | 1,596,429 | 6,248,466 |
| CHANGE IN NET ASSETS | (2,814,913) | (20,004,653) |
| **NET ASSETS, BEGINNING OF YEAR** | 16,287,740 | 36,292,393 |
| **NET ASSETS, END OF YEAR** | $ 13,472,827 | $ 16,287,740 |

*See accompanying Notes to the Financial Statements.*

# RISK MANAGEMENT FUND
# STATEMENTS OF CASH FLOWS
# FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010

| | For the Year Ended June 30, 2011 | For the Year Ended June 30, 2010 |
|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | |
| Receipts from premiums | $ 47,695,000 | $ 27,118,800 |
| Receipts for insurance proceeds | 7,500,000 | 7,861,142 |
| Payments for claims | (48,838,442) | (35,601,367) |
| Payments for administrative expenses | (9,512,163) | (8,989,627) |
| Payments for insurance premiums | (3,929,600) | (3,302,869) |
| **NET CASH FROM OPERATING ACTIVITIES** | (7,085,205) | (12,913,921) |
| **CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES** | | |
| Taxes received | 2,225 | 2,200 |
| **NET CASH FROM NONCAPITAL FINANCING ACTIVITIES** | 2,225 | 2,200 |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | |
| Interest received | 219,778 | 396,266 |
| **NET CASH FROM INVESTING ACTIVITIES** | 219,778 | 396,266 |
| **NET DECREASE IN CASH** | (6,863,202) | (12,515,455) |
| **CASH, BEGINNING OF YEAR** | 114,501,418 | 127,016,873 |
| **CASH, END OF YEAR** | $ 107,638,216 | $ 114,501,418 |
| **RECONCILIATION OF OPERATING LOSS TO NET CASH FROM OPERATING ACTIVITIES** | | |
| **OPERATING LOSS** | $ (4,411,342) | $ (26,253,119) |
| **ADJUSTMENTS TO RECONCILE OPERATING LOSS TO NET CASH FROM OPERATING ACTIVITIES** | | |
| Changes in assets and liabilities | | |
| Increase in accounts receivable | (86,600) | 0 |
| Increase (decrease) in accounts payable | 314,896 | (134,748) |
| Increase (decrease) in claims liability | (2,902,159) | 13,473,946 |
| **TOTAL ADJUSTMENTS** | (2,673,863) | 13,339,198 |
| **NET CASH FROM OPERATING ACTIVITIES** | $ (7,085,205) | $ (12,913,921) |

*See accompanying Notes to the Financial Statements.*

# RISK MANAGEMENT FUND
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010

## A. Summary of Significant Accounting Policies

1. **Reporting Entity –** The Risk Management Fund (RMF) is part of the primary government and has been included in the *Tennessee Comprehensive Annual Financial Report* as an internal service fund.

2. **Measurement Focus and Basis of Accounting –** The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The RMF generally follows private sector standards of accounting and financial reporting issued prior to December 1, 1989, to the extent that these standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. The financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. The RMF distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from the services provided by the RMF. The principal operating revenue of the RMF consists of charges to its customers for insurance premiums. Operating expenses include claims expenses, insurance premiums, administrative expenses and the current charge to the accrued liability. Revenues and expenses not resulting from the services provided by the RMF are reported as nonoperating revenues and expenses.

3. **Cash –** The Risk Management Fund does not maintain its own bank accounts but utilizes the State Pooled Investment Fund for its operating cash needs. The State Pooled Investment Fund is authorized by state statute to invest funds in accordance with policy guidelines approved by the Funding Board of the State of Tennessee. The current resolution of that board gives the Treasurer authority to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, certain repurchase agreements, and various U.S. Treasury and Agency obligations. The State Pooled Investment Fund is also authorized to enter into securities lending agreements in which U.S. Government Securities may be loaned for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities. The State Pooled Investment Fund is not rated by a nationally recognized ratings agency. The investment policy and required risk disclosures relative to the State Pooled Investment Fund are presented on pages 91-95 of this report.

## B. Other Accounting Disclosures

1. **Risk Management –** It is the policy of the state not to purchase commercial insurance for the risks of casualty losses for general liability, automobile liability, professional malpractice, and workers' compensation. The state's management believes it is more economical to manage these risks internally and set aside assets for claim settlement in its internal service fund, the RMF. The state purchases commercial insurance for real property, flood, earthquake, and builder's risk losses and surety bond coverage on the state's officials and employees. The RMF is also responsible for claims for damages to state owned property up to the amount of the property insurance aggregate deductible amount. The insurance policy deductibles vary from $25,000 per occurrence, depending on the type of coverage, to an aggregate of $5 million. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years. All agencies and authorities of the state participate in the RMF, except for the Dairy Promotion Board and the Certified Cotton Growers' Organization. The Tennessee Education Lottery Corporation participates in the RMF for general liability purposes but is responsible for its own worker's compensation coverage.

   The RMF liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported. Because actual claims liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claims liability does

(CONTINUED)

# RISK MANAGEMENT FUND
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010

not necessarily result in an exact amount. Claims liabilities are reevaluated annually to take into consideration recently settled claims, the frequency of claims, and other economic and social factors. The present value of the casualty liability as actuarially determined was $86,167,698 (discounted at 2.00%) at June 30, 2011 and $84,577,236 (discounted at 2.5%) at June 30, 2010. The accrued liability for incurred property losses was $17,559,929 at June 30, 2011 and $22,052,550 at June 30, 2010. The changes in the balances of the claims liabilities during fiscal years 2010 and 2011 were as follows:

| Fiscal Year | Beginning Claims Liability | Current Year Claims and Changes in Estimates | Claim Payments | Advance of Insurance Proceeds | Ending Claims Liability |
|---|---|---|---|---|---|
| 2011 | $106,629,786 | $38,927,980 | ($49,330,139) | $7,500,000 | $103,727,627 |
| 2010 | 93,155,840 | 41,085,822 | (32,611,876) | 5,000,000 | 106,629,786 |

The RMF held $107.6 million in cash at June 30, 2011 and $114.5 million in cash at June 30, 2010 that is designated for payment of these claims.

The RMF allocates the cost of providing claims servicing and claims payment by charging a premium to each agency based on a percentage of each organization's expected loss costs which include both experience and exposures. This charge considers recent trends in actual claims experience of the state as a whole.

2. **Receivable –** The receivables shown on the Statement of Net Assets as due from federal government includes funds to be received from the Federal Emergency Management Agency for property losses that were classified as a disaster.

3. **Insurance Proceeds –** The State suffered a large loss as the result of a flood in May 2010. The state's insurance company provided an advance payment of $7.5 million in fiscal year 2011 and $5 million in fiscal year 2010 to assist the State in its recovery efforts. The flood losses are estimated to be approximately $20 million and the insurance company is responsible for the flood losses exceeding the deductible. These proceeds will be passed on to state agencies as costs related to these losses are incurred. As of June 30, 2011, $5,563,387 had been paid to state agencies for flood losses.

# STATE POOLED INVESTMENT FUND
# INDEPENDENT AUDITOR'S REPORT

STATE OF TENNESSEE
**COMPTROLLER OF THE TREASURY**
DEPARTMENT OF AUDIT / DIVISION OF STATE AUDIT
SUITE 1500, JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-1402
PHONE (615) 401-7897 / FAX (615) 532-2765

December 19, 2011

Members of the General Assembly
and
Members of the State Funding Board
and
The Honorable David H. Lillard, Jr., Treasurer
State Capitol
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying statements of fiduciary net assets of the State Pooled Investment Fund as of June 30, 2011, and June 30, 2010, and the related statements of changes in fiduciary net assets for the years then ended. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the State Funding Board. We do not believe that the Comptroller's service in this capacity affected our ability to conduct an independent audit of the State Pooled Investment Fund.

As discussed in Note A.1., the financial statements referred to above present only the State Pooled Investment Fund of the State of Tennessee and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2011, and June 30, 2010, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the fiduciary net assets of the State Pooled Investment Fund of the State of Tennessee as of June 30, 2011, and June 30, 2010, and the changes in its fiduciary net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with generally accepted government auditing standards, we have also issued our report dated December 19, 2011, on our consideration of the State Pooled Investment Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be considered in assessing the results of our audit.

Sincerely,

Arthur A. Hayes, Jr., CPA
Director

# STATE POOLED INVESTMENT FUND
# STATEMENTS OF FIDUCIARY NET ASSETS
# JUNE 30, 2011 AND JUNE 30, 2010

| | June 30, 2011 | June 30, 2010 |
|---|---|---|
| **ASSETS** | | |
| Cash and cash equivalents | $ 2,261,170,913 | $ 3,866,080,256 |
| Short-term investments, at amortized cost | 4,987,592,606 | 3,037,073,936 |
| Accrued income receivable | 2,629,975 | 2,811,909 |
| **TOTAL ASSETS** | 7,251,393,494 | 6,905,966,101 |
| **LIABILITIES AND NET ASSETS** | | |
| **NET ASSETS HELD IN TRUST FOR POOL PARTICIPANTS** | $ 7,251,393,494 | $ 6,905,966,101 |

*See accompanying Notes to the Financial Statements.*

# STATE POOLED INVESTMENT FUND
# STATEMENTS OF CHANGES IN FIDUCIARY NET ASSETS
# FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010

| | For the Year Ended June 30, 2011 | For the Year Ended June 30, 2010 |
|---|---|---|
| **OPERATIONS** | | |
| Investment income | $ 17,939,345 | $ 26,965,391 |
| Expenses | | |
| Administrative fee | 3,429,925 | 3,386,571 |
| Custodian and banking services fees | 100,968 | 256,744 |
| Total expenses | 3,530,893 | 3,643,315 |
| **NET INVESTMENT INCOME** | 14,408,452 | 23,322,076 |
| **CAPITAL SHARE TRANSACTIONS (DOLLAR AMOUNTS AND NUMBER OF SHARES ARE THE SAME)** | | |
| Shares sold | 41,421,398,801 | 35,065,352,181 |
| Less shares redeemed | 41,090,379,860 | 35,669,172,919 |
| **INCREASE (DECREASE) FROM CAPITAL SHARE TRANSACTIONS** | 331,018,941 | (603,820,738) |
| **TOTAL INCREASE (DECREASE) IN NET ASSETS** | 345,427,393 | (580,498,662) |
| **NET ASSETS HELD IN TRUST FOR POOL PARTICIPANTS** | | |
| **BEGINNING OF YEAR** | 6,905,966,101 | 7,486,464,763 |
| **END OF YEAR** | $ 7,251,393,494 | $ 6,905,966,101 |

*See accompanying Notes to the Financial Statements.*

# STATE POOLED INVESTMENT FUND
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010

## A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. **Reporting Entity –** The State Pooled Investment Fund (SPIF) is an external investment pool sponsored by the State of Tennessee. The external portion of the State Pooled Investment Fund, consisting of funds belonging to entities outside of the State of Tennessee Financial Reporting Entity, has been included as a separate investment trust fund in the *Tennessee Comprehensive Annual Financial Report*. The internal portion, consisting of funds belonging to the State and its component units, has been included in the various participating funds and component units in the *Tennessee Comprehensive Annual Financial Report*.

2. **Measurement Focus and Basis of Accounting –** The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB) using the economic resources measurement focus and the accrual basis of accounting. Under this basis, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

3. **Cash and Cash Equivalents –** This classification includes deposits in demand accounts as well as short-term investments with a maturity date within three months of the date acquired by the State.

4. **Method Used to Report Investments and Participant Shares –** The SPIF is not registered with the Securities and Exchange Commission (SEC) as an investment company but, through its investment policy adopted by the Funding Board of the State of Tennessee (Funding Board), operates in a manner consistent with the SEC's Rule 2a7 of the *Investment Company Act of 1940*. Rule 2a7 allows SEC registered mutual funds to use amortized cost to report net assets in computing share prices. Likewise, the SPIF uses amortized cost accounting measures to report investments and share prices. During the fiscal years ended June 30, 2011 and June 30, 2010, the State had not obtained or provided any legally binding guarantees to support the value of participant shares. The State of Tennessee has not obtained a credit quality rating for the SPIF from a nationally recognized credit ratings agency.

## B. DEPOSITS AND INVESTMENTS

The State Pooled Investment Fund is authorized by statute to invest funds in accordance with policy guidelines approved by the Funding Board. The current resolution of the Funding Board gives the Treasurer approval to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, bonds, notes, and treasury bills of the United States or other obligations guaranteed as to principal and interest by the United States or any of its agencies, repurchase agreements for obligations of the United States or its agencies, and securities lending agreements whereby securities may be loaned for a fee. Investments in derivative type securities and investments of high risk are prohibited.

At June 30, 2011 and June 30, 2010, the principal amount of certificates of deposit in state depositories was $689,105,000 and $992,950,000 respectively. Interest rates on certificates of deposit held at June 30, 2011 ranged from 0.20% to 0.40% and at June 30, 2010 ranged from 0.30% to 0.50%. The days to maturity on certificates of deposit ranged from 7 to 275 days at both June 30, 2011 and at June 30, 2010.

As of June 30, 2011 and June 30, 2010, the SPIF had the following investments:

(*CONTINUED*)

# STATE POOLED INVESTMENT FUND
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010

**June 30, 2011**

| Investment Type | Carrying Amount | Fair Value | Par Value | Interest Rate Range | Days to Maturity | U.S. Treasury (1) | Carrying Amount Credit Quality Ratings: AAA | A1 (2) | Not Rated (3) |
|---|---|---|---|---|---|---|---|---|---|
| Cash Equivalents and Short-term Investments: | | | | | | | | | |
| U.S. Government Agencies | $3,862,483,749 | $3,862,720,440 | $3,856,731,000 | 0.03% - 2.25% | 25 - 410 | | $934,894,622 | | $2,927,589,127 |
| U.S. Government Treasuries | 1,105,065,549 | 1,105,682,080 | 1,106,000,000 | 0.02% - 1.00% | 90 - 344 | $1,105,065,549 | | | |
| Commercial Paper | 859,959,981 | 859,962,000 | 860,000,000 | 0.02% - 0.17% | 1 - 45 | | | $859,959,981 | |
| Total Cash Equivalents and Short-term Investments | 5,827,509,279 | $5,828,364,520 | $5,822,731,000 | | | $1,105,065,549 | $934,894,622 | $859,959,981 | $2,927,589,127 |
| Less: short-term investments classified as cash equivalents on Statement of Fiduciary Net Assets | (1,214,671,673) | | | | | | | | |
| Add: certificates of deposit classified as short-term investments on Statement of Fiduciary Net Assets | 374,755,000 | | | | | | | | |
| Short-term investments as shown on Statement of Fiduciary Net Assets | $4,987,592,606 | | | | | | | | |

(1) Includes obligations of the U.S. Government or obligations explicitly guaranteed by the U.S. Government.

(2) A1 is the highest rating category for commercial paper

(3) Includes securities that are implicitly guaranteed by the U.S. government, but are not rated by Standard and Poor's or Moody's.

**June 30, 2010**

| Investment Type | Carrying Amount | Fair Value | Par Value | Interest Rate Range | Days to Maturity | U.S. Treasury (1) | Carrying Amount Credit Quality Ratings: AAA | A1 (2) | Not Rated (3) |
|---|---|---|---|---|---|---|---|---|---|
| Cash Equivalents and Short-term Investments: | | | | | | | | | |
| U.S. Government Agencies | $3,179,080,555 | $3,180,244,309 | $3,179,314,079 | 0.00% - 1.75% | 7 - 397 | | $1,233,666,647 | | $1,945,413,908 |
| U.S. Government Treasuries | 719,981,683 | 719,971,800 | 720,000,000 | 0.01% - 1.00% | 8 - 22 | $ 719,981,683 | | | |
| Commercial Paper | 1,025,637,933 | 1,025,637,933 | 1,025,700,000 | 0.01% - 0.33% | 1 - 43 | | | $1,025,637,933 | |
| Total Cash Equivalents and Short-term Investments | 4,924,700,171 | $4,925,854,042 | $4,925,014,079 | | | $ 719,981,683 | $1,233,666,647 | $1,025,637,933 | $1,945,413,908 |
| Less: short-term investments classified as cash equivalents on Statement of Fiduciary Net Assets | (2,408,076,235) | | | | | | | | |
| Add: certificates of deposit classified as short-term investments on Statement of Fiduciary Net Assets | 520,450,000 | | | | | | | | |
| Short-term investments as shown on Statement of Fiduciary Net Assets | $3,037,073,936 | | | | | | | | |

(1) Includes obligations of the U.S. Government or obligations explicitly guaranteed by the U.S. Government.

(2) A1 is the highest rating category for commercial paper

(3) Includes securities that are implicitly guaranteed by the U.S. government, but are not rated by Standard and Poor's or Moody's.

**Credit Risk –** Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Credit quality ratings for the SPIF's investments in debt securities as of June 30, 2011 and June 30, 2010 are included in the above schedule. Securities are rated using Standard and Poor's and/or Moody's and are presented above using the Standard and Poor's rating scale. State statutes provide a process for financial institutions desiring to act as state depositories to be approved by the State Treasurer. Statutes also provide for the Commissioner of Financial Institutions to advise, on a timely basis, the Treasurer and the Commissioner of Finance and Administration of the condition of each state bank and state chartered savings and loan association, including his recommendations regarding its condition and safety as a state depository. Similar provisions apply to federally chartered banks and savings and loan associations designated as state depositories. This process ensures that institutions whose financial status is uncertain are monitored for collateral sufficiency. All certificates of deposit are required by policy to be placed directly with state depositories. All repurchase agreements are done with primary dealers in government securities which have executed a master repurchase agreement with the State. The SPIF's investment policy requires a AAA credit quality rating for the purchase of obligations of instrumentalities that are not fully guaranteed by the United States government. Prime banker's acceptances must be issued

(CONTINUED)

## STATE POOLED INVESTMENT FUND
## NOTES TO THE FINANCIAL STATEMENTS
## JUNE 30, 2011 AND JUNE 30, 2010

by domestic banks with a minimum AA long-term debt rating or foreign banks with a AAA long-term debt rating by a majority of the rating services that have rated the issuer. The short-term debt rating must be at least A1 or the equivalent by all of the rating services that rate the issuer. Commercial paper should be rated in the highest tier by all rating agencies that rate the paper. Commercial paper on a credit rating agency's negative credit watch list cannot be purchased under the investment policy. The policy requires that a credit analysis report on the corporation be prepared prior to acquisition of the commercial paper.

**Concentration of Credit Risk –** A concentration of investments in any one single issuer of debt securities presents a greater risk for loss in the event that the issuer fails on its obligations. An objective stated in the SPIF's investment policy is that the investment portfolio will be diversified to avoid incurring unreasonable and avoidable risks regarding specific security types or individual financial institutions. Acquisitions are monitored by policy to assure that no more than twenty percent (20%) of the book value of the pool, at the date of acquisition, is invested in a single United States government agency security and that such acquisition does not cause the SPIF's aggregate United States government agency holdings to exceed fifty percent (50%) of the total book value of the pool on such date. In addition, the SPIF's investment policy limits the book value of prime banker's acceptances to five percent (5%) of the total book value of the pool and limits such investments in any one commercial bank to the lesser of five percent (5%) of the portfolio's book value or $25 million. Prime commercial paper investments are limited to five percent (5%) of the total portfolio book value invested in any one single issuing corporation and the total holdings of an issuer's paper should not represent more than five percent (5%) of the issuing corporation's total outstanding commercial paper, with the maximum amount of a specific corporation's commercial paper limited to $100 million, not including commercial paper maturing on the next business day. Prime commercial paper shall not exceed forty percent (40%) of the total pool's book value. The SPIF had the following investment amounts and percentages of total investments, in organizations representing five percent (5%) or more of total investments, excluding those organizations whose issues are explicitly guaranteed by the United States government, and investments in mutual funds, external investment pools, and other pooled investments:

| June 30,2011 | | |
|---|---|---|
| **Issuer Organization** | **Carrying Amount** | **Percentage of Total Investments** |
| Federal Farmers Credit Banks | $ 1,212,494,243 | 20.81% |
| Federal National Mortgage Association | 1,152,389,012 | 19.77% |
| Federal Home Loan Mortgage Corporation | 1,093,304,313 | 18.76% |
| Federal Home Loan Banks | 404,296,181 | 6.94% |

| June 30,2010 | | |
|---|---|---|
| **Issuer Organization** | **Carrying Amount** | **Percentage of Total Investments** |
| Federal Home Loan Banks | $ 1,113,578,846 | 22.61% |
| Federal National Mortgage Association | 878,799,804 | 17.84% |
| Federal Farmers Credit Banks | 700,023,477 | 14.21% |
| Federal Home Loan Mortgage Corporation | 486,678,428 | 9.88% |
| BNP | 349,999,708 | 7.11% |
| General Electric | 299,987,056 | 6.09% |

(*CONTINUED*)

# STATE POOLED INVESTMENT FUND
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010

**Interest Rate Risk –** Interest rate risk is the risk that future changes in prevailing market rates of interest will have an adverse effect on the fair value of debt investments. The fair values of securities with long terms to maturity may be highly sensitive to interest rate changes. The SPIF's investment policy with respect to maturity states that the dollar weighted average maturity of the pool shall not exceed one hundred twenty (120) days and that no investment may be purchased with a remaining maturity of greater than three hundred ninety seven (397) calendar days. At June 30, 2011, the SPIF held one security which was purchased with a remaining maturity of four hundred ten (410) days which is in violation of the investment policy; however the market value ($50,046,000) was not material . The maximum weighted average maturity of the pool was ninety (90) days until an investment policy change on April 26, 2011. In addition, it is the intent of the Funding Board that the market value of the SPIF not deviate more than one-half percent (0.5%) from amortized cost. If it does, actions may include, but not be limited to, selling securities whose market value substantially deviates from amortized cost, and investing in securities with ninety (90) days or less to maturity. Agency variable rate notes are permitted by investment policy provided they are indexed to treasury bill, commercial paper, federal funds, LIBOR or the prime rates. It is the intent of the Funding Board that variable rate notes must move in the same direction as general money market rates. Prime banker's acceptances must have an original maturity of not more than two hundred seventy (270) days to be eligible for purchase, with the intent to hold to maturity. Prime commercial paper shall not have a maturity that exceeds one hundred eighty (180) days, and individual repurchase agreement transactions shall not have a maturity that exceeds ninety (90) days.

As of June 30, 2011 and June 30, 2010, the SPIF portfolio had the following weighted average maturities on debt investments:

| June 30, 2011 | | |
|---|---|---|
| **Investment Type** | **Carrying Amount** | **Weighted Average Maturity (Months)** |
| U.S. Government Agencies | $3,862,483,749 | 5.11 |
| U.S. Government Treasuries | 1,105,065,549 | 5.47 |
| Commercial Paper | 859,959,981 | 0.45 |
| Total Debt Investments | $5,827,509,279 | 4.48 |
| Total SPIF Portfolio | $7,466,936,136 | 3.70 |

| June 30, 2010 | | |
|---|---|---|
| **Investment Type** | **Carrying Amount** | **Weighted Average Maturity (Months)** |
| U.S. Government Agencies | $3,179,080,555 | 2.43 |
| U.S. Government Treasuries | 719,981,683 | 0.40 |
| Commercial Paper | 1,025,637,933 | 0.47 |
| Total Debt Investments | $4,924,700,171 | 3.42 |
| Total SPIF Portfolio | $6,810,149,992 | 2.80 |

(*CONTINUED*)

# STATE POOLED INVESTMENT FUND
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010

## C. OTHER ACCOUNTING DISCLOSURES

**Description of the State Pooled Investment Fund –** The State Pooled Investment Fund is established by *Tennessee Code Annotated*, Section 9-4-603 "for the purpose of receiving and investing any money in the custody of any officer or officers of the state unless prohibited by statute to be invested." Participants in the SPIF include the general fund of the State and any department or agency of the State which is required by court order, contract, state or federal law or federal regulation to receive interest on invested funds and which are authorized by the State Treasurer to participate in the SPIF. In addition, funds in the State of Tennessee Local Government Investment Pool (LGIP) are consolidated with the SPIF for investment purposes only. The SPIF, as noted in A.4 above, is not registered as an investment company with the SEC. The primary oversight responsibility for the investment and operations of the SPIF rests with the Funding Board.

Investment in the SPIF by local governments and certain state agencies is optional and participants may invest any amount for any length of time in the SPIF. However, some deposits made to the LGIP are contractually required and committed to the State Department of Transportation (DOT). The only withdrawals allowed from these accounts are to pay the DOT in accordance with progress billings for construction projects contracted between the entity and the DOT.

An average rate of return is calculated on the investments made each month in the SPIF and is used to credit earnings to LGIP participants and the State departments and agencies required to earn interest. The State's general fund is credited with the residual earnings. Accordingly, participants' shares are sold and redeemed at a value equal to the amount of the principal plus accrued earnings while investments are reported at amortized cost. For the fiscal years ending June 30, 2011 and June 30, 2010, an administrative fee of .05 percent was charged against each participant's average daily balance to provide funding for administrative expenses to operate the SPIF.

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# INDEPENDENT AUDITOR'S REPORT

STATE OF TENNESSEE
**COMPTROLLER OF THE TREASURY**
DEPARTMENT OF AUDIT / DIVISION OF STATE AUDIT
SUITE 1500, JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-1402
PHONE (615) 401-7897 / FAX (615) 532-2765

December 19, 2011

Members of the General Assembly
and
Members of the Board of Trustees
Tennessee Consolidated Retirement System
and
The Honorable David H. Lillard, Jr., Treasurer
State Capitol
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying statements of plan net assets of the Tennessee Consolidated Retirement System as of June 30, 2011, and June 30, 2010, and the related statements of changes in plan net assets for the years then ended. These financial statements are the responsibility of the Tennessee Consolidated Retirement System's management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the board of trustees of the Tennessee Consolidated Retirement System. We do not believe that the Comptroller's service in this capacity affected our ability to conduct an independent audit of the Tennessee Consolidated Retirement System.

As discussed in Note A.1., the financial statements present only the Tennessee Consolidated Retirement System, pension trust funds of the State of Tennessee, and do not purport to, and do not, present fairly the financial position of the State of Tennessee as of June 30, 2011, and June 30, 2010, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net assets of the Tennessee Consolidated Retirement System as of June 30, 2011, and June 30, 2010, and the changes in its plan net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note A.5., during the year ended June 30, 2010, the Tennessee Consolidated Retirement System implemented Governmental Accounting Standards Board Statement 53, Accounting and Financial Reporting for Derivative Instruments.

(CONTINUED)

## TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
## INDEPENDENT AUDITOR'S REPORT (CONTINUED)

December 19, 2011
Page Two

The management's discussion and analysis and the schedules of funding progress and employer contributions on pages 98 through 103 and 121 through 122 are not required parts of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements. The actuarial balance sheet on page 97 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

In accordance with generally accepted government auditing standards, we have also issued our report dated December 19, 2011, on our consideration of the Tennessee Consolidated Retirement System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with generally accepted government auditing standards and should be considered in assessing the results of our audit.

Sincerely,

Arthur A. Hayes, Jr.

Arthur A. Hayes, Jr., CPA
Director

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010

The Management of the Tennessee Consolidated Retirement System (TCRS) provides this discussion and analysis as an overview of the TCRS' financial activities for the fiscal years ended June 30, 2011 and June 30, 2010. This section should be read in conjunction with the Independent Auditor's Report, the audited financial statements, and the accompanying notes.

## FINANCIAL HIGHLIGHTS

- The plan net assets (total assets minus total liabilities) of the TCRS at June 30, 2011 were $33.7 billion, increasing nearly $5.1 billion (17.8 percent) from the plan net assets at June 30, 2010. The net assets are held in trust to meet future benefit obligations.
- The TCRS relies upon contributions from employees and employers, along with investment income, to meet the funding requirements of an actuarially determined accrued liability. As of July 1, 2009, the date of the latest actuarial valuation, the TCRS' funded ratio was 90.6 percent for the SETHEEPP group and 86.3 percent for the PSPP group.
- Contribution revenue for fiscal year 2011 totaled $1,255,926,943 an increase of 15 percent compared to fiscal year 2010.
- Net investment income for fiscal year 2011 was $5,528,753,502. During fiscal year 2011, the TCRS received an investment return on its portfolio of 19.59 percent, compared to 10.24 percent for fiscal year 2010.
- Total benefits and refunds paid for fiscal year 2011 were $1,688,410,469 – an increase of 7.4 percent over fiscal year 2010 total benefits and refunds paid of $1,571,610,009.
- Total administrative expenses for fiscal year 2011 were $7,156,822 – a 5.1% decrease from fiscal year 2010 administrative expenses of $7,542,822.

## OVERVIEW OF THE FINANCIAL STATEMENTS

The TCRS financial statements consist of the *Statement of Plan Net Assets* (on pages 104 through 105), the *Statement of Changes in Plan Net Assets* (on pages 106 through 107), and the *Notes to the Financial Statements* (on pages 108 through 120). In addition, *Required Supplementary Information* is presented, which includes this *Management's Discussion and Analysis,* as well as the schedules on pages 121 through 122.

The *Statement of Plan Net Assets* and the *Statement of Changes in Plan Net Assets* report information about the plan net assets (total assets in excess of total liabilities) as of the end of the fiscal year and the changes in those plan net assets during the fiscal year. These statements include all assets and liabilities using the accrual basis of accounting. Under the accrual basis of accounting, the current year's revenues and expenses are included in the financial activity, regardless of when cash is received or paid. The difference between the total assets and total liabilities on the *Statement of Plan Net Assets,* or net assets held in trust for pension benefits, provides a measurement of the financial position of the TCRS as of the end of the fiscal year. The *Statement of Changes in Plan Net Assets* provides information on the activities that caused the financial position to change during the fiscal year. Over time, increases or decreases in the plan net assets of the TCRS are one indicator of whether the system's financial health is improving or deteriorating.

(*CONTINUED*)

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# MANAGEMENT'S DISCUSSION AND ANALYSIS
# FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010

In addition to the two basic financial statements, the reader should also review the *Schedules of Funding Progress* and the *Schedules of Employer Contributions* to gain an understanding of the funded status of the TCRS over time. This information provides an indication of the TCRS' ability to meet both current and future benefit payment obligations. The *Notes to the Financial Statements* are also essential to the reader's understanding of the financial statements and provide additional information regarding the TCRS, such as descriptions of the plans administered by the TCRS, including contribution and benefit provisions, and information about the accounting policies and investment activities.

## ANALYSIS OF ASSETS, LIABILITIES AND PLAN NET ASSETS

At June 30, 2011, the TCRS had plan net assets (total assets in excess of total liabilities) of $33.7 billion, an increase of nearly $5.1 billion (17.8 percent) from $28.6 billion at June 30, 2010, following the fiscal year 2010 increase of over $2.2 billion (8.4 percent) from the $26.4 billion of plan net assets as of June 30, 2009. The assets of the TCRS consist primarily of investments. The increase in plan assets is primarily the result of strong investment returns in equity and fixed income markets. Condensed financial information comparing the TCRS' plan net assets for the past three fiscal years follows.

### PLAN NET ASSETS

| | June 30, 2011 | June 30, 2010 | FY11 - FY10 Percentage Change | June 30, 2009 | FY10 - FY09 Percentage Change |
|---|---|---|---|---|---|
| ASSETS | | | | | |
| Cash and cash equivalents | $ 414,134,562 | $ 438,269,286 | (5.5) % | $ 1,267,296,450 | (65.4) % |
| Member and employer receivables | 99,604,471 | 89,310,527 | 11.5 % | 74,112,021 | 20.5 % |
| Investment receivables | 1,431,331,905 | 2,000,061,173 | (28.4) % | 1,373,061,675 | 45.7 % |
| Short-term securities | 0 | 0 | 0.0 % | 391,283,896 | (100.0) % |
| Long-term investments | 33,220,879,536 | 27,911,282,071 | 19.0 % | 24,664,493,110 | 13.2 % |
| Capital assets | 1,896,671 | 0 | - % | 0 | 0.0 % |
| TOTAL ASSETS | 35,167,847,145 | 30,438,923,057 | 15.5 % | 27,770,247,152 | 9.6 % |
| LIABILITIES | | | | | |
| Death benefits, refunds and other payables | 8,544,407 | $8,205,512 | 4.1 % | $7,364,733 | 11.4 % |
| Investment payables | 1,495,994,494 | 1,856,522,455 | (19.4) % | 1,393,656,704 | 33.2 % |
| TOTAL LIABILITIES | 1,504,538,901 | 1,864,727,967 | (19.3) % | 1,401,021,437 | 33.1 % |
| NET ASSETS HELD IN TRUST FOR PENSION BENEFITS | $ 33,663,308,244 | $ 28,574,195,090 | 17.8 % | $ 26,369,225,715 | 8.4 % |

(CONTINUED)

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010

## ANALYSIS OF REVENUES AND EXPENSES

Contributions to TCRS had a larger than normal increase of $164.1 million (15%) over contributions for fiscal year 2010 due to the change in employer contribution rates effective July 1, 2010. With the continued increase of investment income of $2.8 billion (105.4%) for fiscal year 2011 compared to investment income for fiscal year 2010, the overall increase in revenues for 2011 was 79.3% compared to revenues for fiscal year 2010. Employer contribution rates for the TCRS did not change during fiscal year 2010; therefore, the slight change of .1% in contributions from fiscal year 2009 to fiscal year 2010 was due to changes in salary.

Investment expenses for fiscal year 2011 increased $3.4 million (11.8 %) due to the continued market appreciation in the externally managed assets in 2011. Improved market conditions in fiscal year 2011 resulted in an overall gain to the TCRS investment portfolio of 19.59% and net investment income of $5.5 billion. Net investment income for fiscal year 2010 was $2.7 billion due to the start of the improved market conditions in fiscal year 2010.

Total benefits and refunds paid during the year ended June 30, 2011 were $1,688,410,470, an increase of 7.4 percent over fiscal year 2010 total benefits and refunds paid. Total benefits and refunds paid during the year ended June 30, 2010 were $1,571,610,009, an increase of 5.5 percent over fiscal year 2009 total benefits and refunds paid. The increase in benefit expenses for fiscal year 2011 is attributed to 2.7 percent in cost of living adjustments awarded to retirees on July 1, 2010, as well as more retirees being added to payroll than removed during this fiscal year. The increase in benefit expenses in fiscal year 2010 can be attributed to more retirees being added to payroll than removed during this fiscal year. Total refunds paid decreased $883,258 (2.4%) in fiscal year 2011 from fiscal year 2010. Total refunds paid had increased $4.4 million (13.7%) in fiscal year 2010 over fiscal year 2009 and were attributed to the weak economy where more terminated members are choosing to withdraw from the system instead of leaving the funds invested.

Administrative expenses for the year ended June 30, 2011 were $7,156,822, a decrease of 5.1 percent from fiscal year 2010 administrative expenses. The decrease was primarily due to the additional expense of the biennial actuarial study performed in fiscal year 2010 and not being performed in fiscal year 2011. Administrative expenses for the year ended June 30, 2010 were $7,542,822, an increase of 4.7 percent over fiscal year 2009 administrative expenses.

Condensed financial information comparing the TCRS' revenues and expenses for the past three fiscal years follows.

(*CONTINUED*)

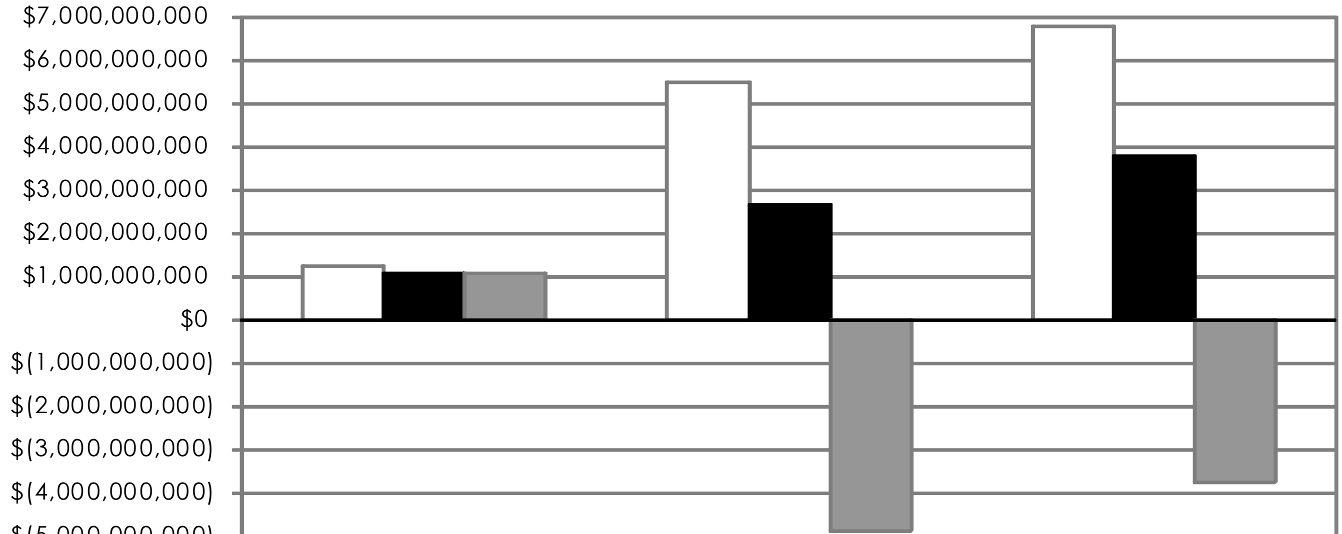
# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# MANAGEMENT'S DISCUSSION AND ANALYSIS
# FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010

## CHANGES IN PLAN NET ASSETS

| | For the Year Ended June 30, 2011 | For the Year Ended June 30, 2010 | FY11 - FY10 Percentage Change | For the Year Ended June 30, 2009 | FY10 - FY09 Percentage Change |
|---|---|---|---|---|---|
| **ADDITIONS** | | | | | |
| Contributions | $1,255,926,943 | $1,091,776,287 | 15.0 % | $1,090,470,093 | 0.1 % |
| **Investment income** | | | | | |
| Net appreciation (depreciation) in fair value of investments | $4,597,653,001 | 1,802,314,559 | 155.1 % | (5,855,240,629) | 130.8 % |
| Interest, dividends and other investment income | $963,313,744 | 918,842,338 | 4.8 % | 1,018,043,263 | (9.7) % |
| Less: Investment expense | ($32,213,243) | (28,810,978) | 11.8 % | (21,288,813) | 35.3 % |
| Net investment income | $5,528,753,502 | 2,692,345,919 | 105.4 % | (4,858,486,179) | 155.4 % |
| **TOTAL ADDITIONS** | $6,784,680,445 | 3,784,122,206 | 79.3 % | (3,768,016,086) | 200.4 % |
| **DEDUCTIONS** | | | | | |
| Annuity benefits | | | | | |
| Retirement benefits | $1,248,538,286 | 1,164,713,725 | 7.2 % | 1,083,753,159 | 7.5 % |
| Survivor benefits | $76,298,394 | 71,380,041 | 6.9 % | 66,732,833 | 7.0 % |
| Disability benefits | $32,140,006 | 30,500,247 | 5.4 % | 29,607,231 | 3.0 % |
| Cost of living | $290,396,251 | 261,479,337 | 11.1 % | 271,845,658 | (3.8) % |
| Death benefits | $5,498,139 | 7,114,008 | (22.7) % | 5,724,443 | 24.3 % |
| Refunds | $35,539,393 | 36,422,651 | (2.4) % | 32,021,785 | 13.7 % |
| Administrative expenses | $7,156,822 | 7,542,822 | (5.1) % | 7,202,572 | 4.7 % |
| **TOTAL DEDUCTIONS** | $1,695,567,291 | 1,579,152,831 | 7.4 % | 1,496,887,681 | 5.5 % |
| **NET INCREASE (DECREASE)** | $5,089,113,154 | 2,204,969,375 | 130.8 % | (5,264,903,767) | 141.9 % |
| **NET ASSETS HELD IN TRUST FOR PENSION BENEFITS BEGINNING OF YEAR** | $28,574,195,090 | 26,369,225,715 | 8.4 % | 31,634,129,482 | (16.6) % |
| **END OF YEAR** | $33,663,308,244 | $28,574,195,090 | 17.8 % | $26,369,225,715 | 8.4 % |

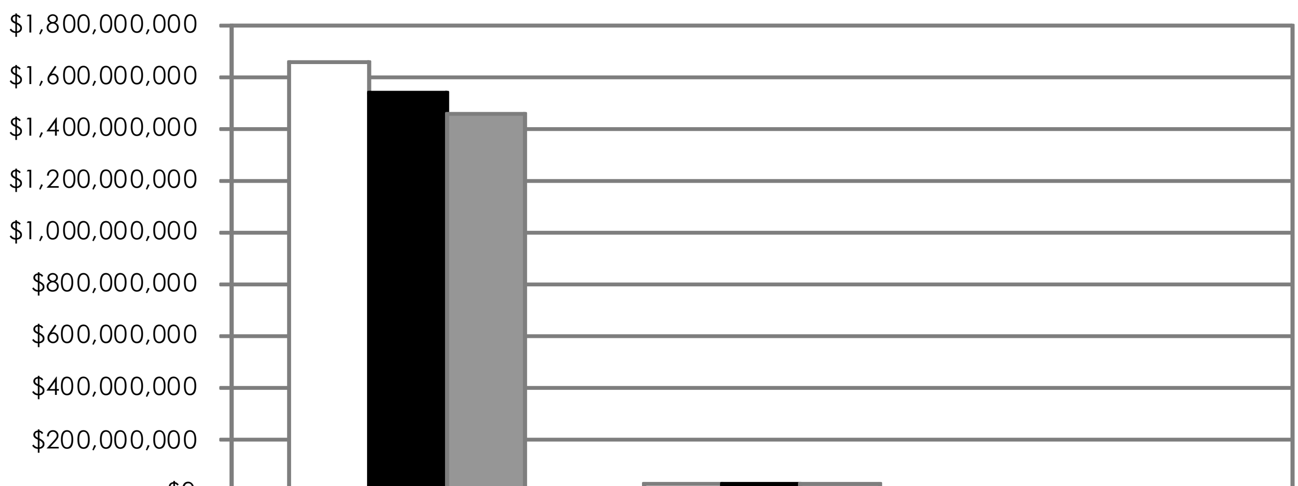
# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# MANAGEMENT'S DISCUSSION AND ANALYSIS
# FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010

## REVENUES BY TYPE




| | Contributions | Net Investment Income | Total Additions |
|---|---|---|---|
| Year Ended 6/30/11 | $1,255,926,943 | $5,528,753,502 | $6,784,680,445 |
| Year Ended 6/30/10 | $1,091,776,287 | $2,692,345,919 | $3,784,122,206 |
| Year Ended 6/30/09 | $1,090,470,093 | $(4,858,486,179) | $(3,768,016,086) |

## EXPENSES BY TYPE




| | Benefit Payments | Refunds | Administrative |
|---|---|---|---|
| Year Ended 6/30/11 | $1,652,871,076 | $35,539,393 | $7,156,822 |
| Year Ended 6/30/10 | $1,535,187,358 | $36,422,651 | $7,542,822 |
| Year Ended 6/30/09 | $1,457,663,324 | $32,021,785 | $7,202,572 |

(CONTINUED)

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# MANAGEMENT'S DISCUSSION AND ANALYSIS
# FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010

## ECONOMIC FACTORS, FUTURE FUNDING PROVISIONS, OVERALL OUTLOOK

For the year ended June 30, 2011, the portfolio delivered an exceptional return of 19.59% which was the strongest annual return for the fund since 1986. All major asset classes contributed significantly to the performance of the fund for the fiscal year.

The domestic equity portfolio generated 33.71% building on an increase of 13.73% from the prior year. The S&P 1500 index reported a gain of 31.65% for the fiscal year ended June 30, 2011. The international stock portfolio gained 33.01% for the year following the gain of 9.73% for the year ended June 30, 2010. The international equity market, as represented by the EAFE IMI index, reported a gain of 31.05% in the fiscal year ended June 30, 2011. Domestic fixed income returned 6% for the year and the portfolio transitioned from the use of the Citigroup Broad Investment Graded Index to the Citigroup Large Pension Fund Index. The Large Pension Fund Index returned 3.79% during the fiscal year while the Broad Investment Grade Index returned 3.66%. The Real Estate Portfolio gained 15.50% for the 2011 fiscal year which followed a loss of 16.33% in fiscal year 2010.

Equity and fixed income markets performed extremely well in the 2011 fiscal year largely as the result of significant monetary stimulus in the first quarter of the year along with generalized slow improvement in economic activity. However, the environment was characterized by signs of cyclical economic improvement somewhat offset by continuing deflationary pressures resulting from declining levels of private sector indebtedness. Dramatic monetary support appeared to provide a floor for economic activity during the year. While the overall economic and market outlook has improved, significant questions remain about the vitality and durability of the current rebound.

An actuarial valuation was performed as of July 1, 2009. The employer contribution rates determined in this valuation were effective July 1, 2010. The required contributions to the plan increased primarily due to investment returns and mortality improvements.

In December 2010, TCRS contracted with Deloitte Consulting, LLC, to provide a new pension administration system to replace the retirement information system. The new pension administration system, referred to as Concord, will replace five separate operating systems with one integrated web-based system that will greatly improve the level of service we provide to our members and employers. The multi-year Concord project will be implemented in three major phases: document imaging, retired payroll, and active member. Software development costs have been capitalized and will be amortized over the useful life of the system once the system has been fully implemented.

## CONTACTING THE TCRS

This report is designed to provide a financial overview of the TCRS to state legislators, members of the Board of Trustees of the TCRS, state officials, participating employers and any other interested parties. Questions or requests for additional information regarding the financial information presented in this report may be addressed in writing to the Tennessee Treasury Department, Consolidated Retirement System, 502 Deaderick Street, Nashville, TN 37243-0201.

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# STATEMENTS OF PLAN NET ASSETS
# JUNE 30, 2011 AND JUNE 30, 2010

| *Expressed in Thousands* | State Employees, Teachers, Higher Education Employees Pension Plan (SETHEEPP) | Political Subdivisions Pension Plan (PSPP) |
|---|---|---|
| ASSETS | | |
| Cash and cash equivalents | $ 340,115 | $ 74,019 |
| Receivables | | |
| Member receivable | 19,570 | 5,266 |
| Employer receivable | 53,975 | 20,793 |
| Accrued interest receivable | 84,099 | 18,302 |
| Accrued dividends receivable | 39,371 | 8,569 |
| Real estate income receivable | 50 | 11 |
| Derivative instruments receivable | 319,386 | 69,508 |
| Investments sold | 732,599 | 159,437 |
| Total receivables | 1,249,050 | 281,886 |
| Investments, at fair value | | |
| Government securities | 7,135,403 | 1,552,887 |
| Corporate securities | 4,554,482 | 991,198 |
| Corporate stocks | 14,640,474 | 3,186,225 |
| Derivative instruments | 9 | 2 |
| Private Equities | 61,296 | 13,340 |
| Real estate | 891,538 | 194,026 |
| Total investments | 27,283,202 | 5,937,678 |
| Capital Assets, at cost | | |
| Intangible Asset | 1,558 | 339 |
| TOTAL ASSETS | 28,873,925 | 6,293,922 |
| LIABILITIES | | |
| Accounts payable | | |
| Death benefits and refunds payable | 1,108 | 899 |
| Retiree insurance premium payable | 5,290 | 1,151 |
| Other | 97 | 0 |
| Investments purchased | 904,384 | 196,823 |
| Derivative instruments payable | 318,780 | 69,376 |
| Other investment payables | 5,446 | 1,185 |
| TOTAL LIABILITIES | 1,235,105 | 269,434 |
| NET ASSETS HELD IN TRUST FOR PENSION BENEFITS | $ 27,638,820 | $ 6,024,488 |

*See accompanying Notes to the Financial Statements.*

(CONTINUED)

| June 30, 2011 Total | State Employees, Teachers, Higher Education Employees Pension Plan (SETHEEPP) | Political Subdivisions Pension Plan (PSPP) | June 30, 2010 Total |
|---|---|---|---|
| $ 414,134 | $ 362,240 | $ 76,029 | $ 438,269 |
| 24,836 | 22,006 | 4,957 | 26,963 |
| 74,768 | 43,752 | 18,596 | 62,348 |
| 102,401 | 88,666 | 18,610 | 107,276 |
| 47,940 | 25,731 | 5,400 | 31,131 |
| 61 | 75 | 16 | 91 |
| 388,894 | 557,809 | 117,075 | 674,884 |
| 892,036 | 980,820 | 205,859 | 1,186,679 |
| 1,530,936 | 1,718,859 | 370,513 | 2,089,372 |
| 8,688,290 | 7,142,965 | 1,499,198 | 8,642,163 |
| 5,545,680 | 4,406,274 | 924,808 | 5,331,082 |
| 17,826,699 | 10,690,206 | 2,243,709 | 12,933,915 |
| 11 | 3,524 | 740 | 4,264 |
| 74,636 | 21,996 | 4,617 | 26,613 |
| 1,085,564 | 804,412 | 168,833 | 973,245 |
| 33,220,880 | 23,069,377 | 4,841,905 | 27,911,282 |
| 1,897 | 0 | 0 | 0 |
| 35,167,847 | 25,150,476 | 5,288,447 | 30,438,923 |
| 2,007 | 1,000 | 792 | 1,792 |
| 6,441 | 5,137 | 1,078 | 6,215 |
| 97 | 198 | 0 | 198 |
| 1,101,207 | 969,207 | 203,422 | 1,172,629 |
| 388,156 | 560,589 | 117,659 | 678,248 |
| 6,631 | 4,667 | 979 | 5,646 |
| 1,504,539 | 1,540,798 | 323,930 | 1,864,728 |
| $ 33,663,308 | $ 23,609,678 | $ 4,964,517 | $ 28,574,195 |

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# STATEMENTS OF CHANGES IN PLAN NET ASSETS
# FOR THE YEARS ENDED JUNE 30, 2011 AND JUNE 30, 2010

| *Expressed in Thousands* | State Employees, Teachers, Higher Education Employees Pension Plan (SETHEEPP) | Political Subdivisions Pension Plan (PSPP) |
|---|---|---|
| ADDITIONS | | |
| Contributions | | |
| Member contributions | $ 192,467 | $ 67,920 |
| Employer contributions | 721,759 | 273,781 |
| Total contributions | 914,226 | 341,701 |
| Investment income | | |
| Net appreciation in fair value of investments | 3,785,947 | 811,706 |
| Interest | 462,425 | 99,143 |
| Dividends | 277,650 | 59,528 |
| Real estate income, net of operating expenses | 53,168 | 11,399 |
| Total investment income | 4,579,190 | 981,776 |
| Less: Investment expense | (26,453) | (5,760) |
| Net investment income | 4,552,737 | 976,016 |
| TOTAL ADDITIONS | 5,466,963 | 1,317,717 |
| DEDUCTIONS | | |
| Annuity benefits | | |
| Retirement benefits | 1,062,838 | 185,700 |
| Survivor benefits | 64,950 | 11,348 |
| Disability benefits | 27,360 | 4,780 |
| Cost of living | 256,137 | 34,259 |
| Death benefits | 4,054 | 1,444 |
| Refunds | 18,957 | 16,583 |
| Administrative expense | 3,525 | 3,632 |
| TOTAL DEDUCTIONS | 1,437,821 | 257,746 |
| NET INCREASE | 4,029,142 | 1,059,971 |
| NET ASSETS HELD IN TRUST FOR PENSION BENEFITS | | |
| BEGINNING OF YEAR | 23,609,678 | 4,964,517 |
| END OF YEAR | $27,638,820 | $6,024,488 |

*See accompanying Notes to the Financial Statements.*

(CONTINUED)

| For the Year Ended June 30, 2011 Total | State Employees, Teachers, Higher Education Employees Pension Plan (SETHEEPP) | Political Subdivisions Pension Plan (PSPP) | For the Year Ended June 30, 2010 Total |
|---|---|---|---|
| $ 260,387 | $ 190,635 | $ 64,414 | $ 255,049 |
| 995,540 | 578,403 | 258,324 | 836,727 |
| 1,255,927 | 769,038 | 322,738 | 1,091,776 |
| | | | |
| 4,597,653 | 1,494,405 | 307,909 | 1,802,314 |
| 561,568 | 482,315 | 99,369 | 581,684 |
| 337,178 | 226,610 | 46,687 | 273,297 |
| 64,567 | 52,952 | 10,910 | 63,862 |
| 5,560,966 | 2,256,282 | 464,875 | 2,721,157 |
| (32,213) | (23,877) | (4,934) | (28,811) |
| 5,528,753 | 2,232,405 | 459,941 | 2,692,346 |
| | | | |
| 6,784,680 | 3,001,443 | 782,679 | 3,784,122 |
| | | | |
| 1,248,538 | 994,439 | 170,275 | 1,164,714 |
| 76,298 | 60,945 | 10,435 | 71,380 |
| 32,140 | 26,041 | 4,459 | 30,500 |
| 290,396 | 231,084 | 30,395 | 261,479 |
| 5,498 | 4,694 | 2,420 | 7,114 |
| 35,540 | 19,371 | 17,052 | 36,423 |
| 7,157 | 3,924 | 3,619 | 7,543 |
| | | | |
| 1,695,567 | 1,340,498 | 238,655 | 1,579,153 |
| 5,089,113 | 1,660,945 | 544,024 | 2,204,969 |
| 28,574,195 | 21,948,733 | 4,420,493 | 26,369,226 |
| $ 33,663,308 | $ 23,609,678 | $ 4,964,517 | $ 28,574,195 |

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM NOTES TO THE FINANCIAL STATEMENTS JUNE 30, 2011 AND JUNE 30, 2010

The Tennessee Consolidated Retirement System (TCRS) administers two defined benefit pension plans - State Employees, Teachers and Higher Education Employees Pension Plan (SETHEEPP) and Political Subdivisions Pension Plan (PSPP). Although the assets of the plans are commingled for investment purposes, each plan's assets may be used only for the payment of benefits to members of that plan, in accordance with the terms of the plan.

## A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. **Reporting Entity –** The TCRS is included in the State of Tennessee Financial Reporting Entity. Because of the state's fiduciary responsibility, the TCRS has been included as pension trust funds in the *Tennessee Comprehensive Annual Financial Report.*

2. **Measurement Focus and Basis of Accounting –** The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The financial statements have been prepared using the flow of economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

   Plan member contributions are recognized in the period of time for which the contributions are assessed. Plan employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each plan.

3. **Cash and Cash Equivalents –** Cash and cash equivalents by definition, includes cash and short-term investments with a maturity date within three months of the acquisition date. The state's accounting policy regarding the definition of cash and cash equivalents includes cash management pools as cash. Cash received by the TCRS that cannot be invested immediately in securities, or that is needed for operations, is invested in the State Pooled Investment Fund sponsored by the State of Tennessee and administered by the State Treasurer. The classification of cash and cash equivalents also includes cash invested in a short-term, open-end mutual fund under the contractual arrangement for master custody services.

4. **Method Used to Value Investments –** Investments are reported at fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. The fair value of real estate investments is determined at least every three years by qualified independent appraisers who are members of the Appraisal Institute and internally by real estate advisors for those years when independent appraisals are not performed. The fair value of private equity investments is determined by the fund managers using various methodologies as applicable under Generally Accepted Accounting Principles. In many cases, these valuations are additionally reviewed by advisory boards comprised of a subgroup of the fund's investors. These valuations are audited on an annual basis by independent accounting firms engaged by the private equity fund managers Investment income includes realized and unrealized appreciation (depreciation) in the fair value of investments. Interest income is recognized when earned. Securities and securities transactions are recorded in the financial statements on trade-date basis. Real estate transactions are recorded in the financial statements at the time of closing.

5. **Capital Assets –** Capital assets consist of internally generated computer software in development and are reported at historical cost. Capital assets are defined by the state as assets with an initial individual cost of $5,000 or more and an estimated useful life in excess of two years. Software in development was

*(CONTINUED)*

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010 (CONTINUED)

valued at June 30, 2009 and June 30, 2010 at zero and at June 30, 2011 was valued at $1,896,671. Software in development will be depreciated over the ten year estimated life of the system once the system is completely operational.

## B. PLAN DESCRIPTIONS AND CONTRIBUTION INFORMATION

At July 1, 2009, the date of the latest actuarial valuation, the membership of each plan consisted of the following:

| | SETHEEPP | PSPP |
|---|---|---|
| Retirees and beneficiaries currently receiving benefits | 76,955 | 30,920 |
| Terminated members entitled to but not receiving benefits | 21,577 | 8,823 |
| Current active members | 136,147 | 78,803 |
| Total | 234,679 | 118,546 |
| Number of participating employers | 140 | 482 |

### State Employees, Teachers and Higher Education Employees Pension Plan

*Plan Description* – SETHEEPP is a cost-sharing, multiple employer defined benefit pension plan that covers the employees of the state, teachers with Local Education Agencies (LEA's) and higher education employees. The TCRS provides retirement benefits as well as death and disability benefits to plan members and their beneficiaries. Benefits are determined by a formula using the member's high five-year average salary and years of service. Members become eligible to retire at the age of 60 with five years of service or at any age with 30 years of service. A reduced retirement benefit is available to vested members who are at least 55 years of age or have 25 years of service. Disability benefits are available to active members with five years of service who become disabled and cannot engage in gainful employment. There is no service requirement for disability that is the result of an accident or injury occurring while the member was in the performance of duty. Members joining the plan on or after July 1, 1979 are vested after five years of service. Members joining prior to July 1, 1979 are vested after four years of service. Compounded cost of living adjustments (COLA) are provided each July based on the percentage change in the Consumer Price Index (CPI) during the previous calendar year except that (a) no COLA is granted if the CPI is less than one-half percent; (b) a COLA of 1 percent will be granted if the CPI increases between one-half percent and one percent; and (c) the maximum annual COLA is capped at three percent. Benefit provisions are established by state statute found in Title Eight, Chapters 34 through 37 of the *Tennessee Code Annotated*. State statutes are amended by the Tennessee General Assembly. Ad hoc increases may only be authorized by the General Assembly. Public safety officers receive an additional supplemental benefit that is paid from age 60 to age 62.

*Superseded Systems and Certain Employment Classifications* – Members of superseded systems that became members of the TCRS at consolidation in 1972, have their rights preserved to the benefits of the superseded system, if the benefit from the superseded plan exceeds that provided by the Group 1 (teachers and general employees) TCRS formula. Likewise, public safety employees and officials of TCRS Groups 2, 3 and 4 are entitled to the benefits of those formulas, if better than the Group 1 benefits.

*Contributions and Reserves* – Effective July 1, 1981, the plan became noncontributory for most state and higher education employees. The contribution rate for teachers is five percent of gross salary. The employers contribute a set percentage of their payrolls, determined by an actuarial valuation. *Tennessee Code Annotated* Title Eight, Chapter 37 provides that the contribution rates be established and may be amended by the Board of Trustees of the TCRS. The administrative budget for the plan is approved through the state of Tennessee's annual budget process. Funding for the administrative budget is included in employer contributions.

(CONTINUED)

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM NOTES TO THE FINANCIAL STATEMENTS JUNE 30, 2011 AND JUNE 30, 2010 (CONTINUED)

The net assets of the plan are legally required to be reserved in two accounts, the Member Reserve and the Employer Reserve. The Member Reserve represents the accumulation of employee contributions plus interest. The Employer Reserve represents the accumulation of employer contributions, investment income and transfers from the Member Reserve for retiring members. Benefit payments and interest credited to the members' accounts are reductions to the Employer Reserve. At June 30, 2011, the plan's Member Reserve and Employer Reserve were fully funded with balances of $3.7 billion and $23.93 billion, respectively. At June 30, 2010, the plan's Member Reserve and Employer Reserve were fully funded with balances of $3.62 billion and $19.98 billion, respectively.

**Political Subdivisions Pension Plan**

*Plan Description* – PSPP is an agent multiple-employer defined benefit pension plan that covers the employees of participating political subdivisions of the state of Tennessee. Employee class differentiations are not made under PSPP. The TCRS provides retirement benefits as well as death and disability benefits to plan members and their beneficiaries. Benefits are determined by a formula using the member's high five-year average salary and years of service. Members become eligible to retire at the age of 60 with five years of service or at any age with 30 years of service. A reduced retirement benefit is available to vested members who are at least 55 years of age or have 25 years of service. Disability benefits are available to active members with five years of service who become disabled and cannot engage in gainful employment. There is no service requirement for disability that is the result of an accident or injury occurring while the member was in the performance of duty. Members joining the plan prior to July 1, 1979 are vested after four years of service. Members joining on or after July 1, 1979 are vested upon completion of 10 years of service, unless five years vesting is authorized by resolution of the chief governing body. Cost of living adjustments (COLA) are the same as provided by SETHEEPP except that the local government may elect (a) to provide no COLA benefits or (b) to provide COLA benefits under a non-compounding basis rather than the compounded basis applicable under SETHEEPP. Benefit provisions are established and amended by state statute. Pursuant to Article Two, Section 24 of the *Constitution of the State of Tennessee*, the state cannot mandate costs on local governments. Any benefit improvement may be adopted by the governing body of a governmental entity participating in the TCRS.

*Contributions and Reserves* – Political subdivisions may elect contributory or noncontributory retirement for their employees. The contribution rate for contributory employees of political subdivisions is five percent of gross salary. The employers contribute a set percentage of their payrolls, equal to at least, the percentage determined by an actuarial valuation. State statute provides that the contribution rates be established and may be amended by the Board of Trustees of the TCRS. The administrative budget for the plan is approved through the state's annual budget process. Funding for the administrative budget is included in employer contributions.

The net assets of the plan are legally required to be reserved in two accounts, the Member Reserve and the Employer Reserve. The Member Reserve represents the accumulation of employee contributions plus interest. The Employer Reserve represents the accumulation of employer contributions, investment income and transfers from the Member Reserve for retiring members. Benefit payments and interest credited to the members' accounts are reductions to the Employer Reserve. At June 30, 2011, the plan's Member Reserve and Employer Reserve were fully funded with balances of $1.1 billion and $4.92 billion, respectively. At June 30, 2010, the plan's Member Reserve and Employer Reserve were fully funded with balances of $1.05 billion and $3.91 billion, respectively.

## C. DEPOSITS AND INVESTMENTS

State statute authorizes the TCRS to maintain cash, not exceeding ten percent of the total amount of funds in the retirement system, on deposit in one or more banks, savings and loan associations or trust companies

(CONTINUED)

## TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
## NOTES TO THE FINANCIAL STATEMENTS
## JUNE 30, 2011 AND JUNE 30, 2010 (CONTINUED)

that are qualified as state depositories. The TCRS does not utilize its own bank accounts but invests in the State Pooled Investment Fund for the initial deposit of funds and for its operating cash needs. The State Pooled Investment Fund is authorized by state statute to invest funds in accordance with policy guidelines approved by the Funding Board of the State of Tennessee. The current resolution of that board gives the Treasurer authority to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, certain repurchase agreements and various U.S. Treasury and Agency obligations. The State Pooled Investment Fund is also authorized to enter into securities lending agreements in which U.S. Government Securities may be loaned for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities.

State statute also authorizes the TCRS to invest in bonds, debentures, preferred stock and common stock, real estate and in other good and solvent securities subject to the approval of the Board of Trustees, but further subject to the following statutory restrictions and provisions:

a. The total sum invested in common and preferred stocks shall not exceed seventy-five percent (75 percent) of the total of the funds of the retirement system.

b. The total sum invested in notes and bonds or other fixed income securities exceeding one year in maturity shall not exceed seventy-five percent (75 percent) of the total funds of the retirement system.

c. Within the restrictions in (a) and (b) above, an amount not to exceed fifteen percent (15 percent) of the total of the funds of the retirement system may be invested in securities of the same kinds, classes, and investment grades as those otherwise eligible for investment in various approved foreign countries, provided that such percentage may be increased by the board with the subsequent approval of the council on pensions and insurance.

d. Within the restrictions in (a) and (b) above, funds may be invested in Canadian securities which are substantially of the same kinds, classes and investment grades as those otherwise eligible for investment.

e. The total amount of securities loaned under a securities lending program cannot exceed thirty percent (30 percent) of total assets.

f. The total sum invested in real estate shall not exceed ten percent (10 percent) of the market value of total assets.

g. The total sum invested in private equities shall not exceed five percent (5 percent) of the market value of total assets.

State statute also authorizes the TCRS to invest in forward contracts to hedge its foreign currency exposure and to purchase or sell domestic equity index futures contracts for the purpose of asset allocation relating to the domestic equity portfolio. The total amount of the financial futures contract obligation shall not exceed five percent (5 percent) of the market value of total assets. Gross exposure to approved fixed income financial instruments will be limited to 10% of the market value of the System's total assets for risk mitigating positions and 10% for risk positions. Position sizes will be measured by notional amounts. Options will be measured in their notional equivalents.

Title to real property invested in by the TCRS is held by real estate investment holding companies.

As of June 30, 2011 and June 30, 2010, the TCRS had the following investments:

*(CONTINUED)*

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010 (CONTINUED)

## Investments
*(Expressed in Thousands)*

**2011**

| Investment Type | Fair Value as of June 30, 2011 | U.S. Treasury Agency (1) | Credit Quality Ratings | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | AAA | AA | A | BBB | BB | B | CCC | CC | D | A1 (3) | Not Rated |
| Debt Investments | | | | | | | | | | | | | |
| U.S. Govt. Agencies | $ 311,472 | $ 102,034 | $ 164,431 | $ 16,960 | | | | | | | | | $ 28,047 (2) |
| U.S. Govt. Inflation Indexed | 2,475,914 | 2,475,914 | | | | | | | | | | | |
| U.S. Govt. Treasuries, Notes, Bonds | 1,355,666 | 1,345,642 | 10,024 | | | | | | | | | | |
| U. S. Govt. Asset Backed | 117,625 | 117,625 | | | | | | | | | | | |
| Municipal Bonds | 149,480 | | 32,649 | 55,086 | $ 61,745 | | | | | | | | |
| Govt. Mortgage Backed | 3,667,503 | 437,001 | 26,576 | | | | | | | | | | 3,203,926 (2) |
| Commercial Mortgage Backed | 381,608 | | 306,660 | 64,905 | 10,043 | | | | | | | | |
| Corporate CMO's | 313,391 | | 56,374 | | | | $ 2,021 | $68,922 | $156,593 | $15,529 | $10,077 | | 3,875 |
| Corporate Bonds | 3,764,808 | | 138,541 | 290,304 | 1,117,282 | $1,967,171 | 168,915 | 28,325 | | 1,201 | | | 53,069 |
| Corporate Asset Backed | 1,015,712 | | 769,168 | 123,431 | 70,559 | 41,765 | | | 9,152 | | | | 1,637 |
| Non-U.S. Govt./Sovereign | 610,630 | | 290,256 | 320,374 | | | | | | | | | |
| Short-Term Commercial Paper | 388,064 | | | | | | | | | | | $388,064 | |
| Total Debt Investments | $ 14,551,873 | $4,478,216 | $1,794,679 | $871,060 | $1,259,629 | $2,008,936 | $170,936 | $97,247 | $165,745 | $16,730 | $10,077 | $388,064 | $3,290,554 |
| Other Investments | | | | | | | | | | | | | |
| U.S. Equity | $ 11,399,485 | | | | | | | | | | | | |
| Non-U.S. Equity | 6,497,376 | | | | | | | | | | | | |
| Derivatives | 11 | | | | | | | | | | | | |
| Real Estate | 1,085,564 | | | | | | | | | | | | |
| Private Equities | 74,636 | | | | | | | | | | | | |
| Money Market Funds (not rated) | 113,893 | | | | | | | | | | | | |
| Total Other Investments | $ 19,170,965 | | | | | | | | | | | | |
| Total Investments | $ 33,722,838 | | | | | | | | | | | | |
| Less: Short-term Investments Classified as Cash Equivalent on the Statements of Plan Net Assets | (501,958) | | | | | | | | | | | | |
| Total Investments as Shown on Statements of Plan Net Assets | $ 33,220,880 | | | | | | | | | | | | |

(1) Includes obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government.

(2) Includes securities that are implicitly guaranteed by the U.S. government, but are not rated by Standard and Poor's or Moody's.

(3) A1 is the highest rating category for commercial paper.

(CONTINUED)

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010 (CONTINUED)

## Investments
*(Expressed in Thousands)*

**2010**

| Investment Type | Fair Value as of June 30, 2010 | U.S. Treasury Agency (1) | Credit Quality Ratings | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | AAA | AA | A | BBB | BB | B | CCC | CC | A1 (3) | Not Rated |
| Debt Investments | | | | | | | | | | | | |
| U.S. Govt. Agencies | $ 449,980 | | | | | | | | | | | $ 449,980 (2) |
| U.S. Govt. Inflation Indexed | 2,331,362 | $2,331,362 | | | | | | | | | | |
| U.S. Govt. Treasuries, Notes, Bonds | 1,280,095 | 1,270,056 | $ 10,039 | | | | | | | | | |
| U. S. Govt. Asset Backed | 141,172 | 141,172 | | | | | | | | | | |
| Municipal Bonds | $104,066 | | | $ 42,709 | $ 61,357 | | | | | | | |
| Govt. Mortgage Backed | 3,227,126 | 511,824 | | | | | | | | | | 2,715,302 (2) |
| Commercial Mortgage Backed | 454,043 | | 383,543 | 51,718 | 18,782 | | | | | | | |
| Corporate CMO's | 410,479 | | 63,468 | | | | $ 18,065 | $ 90,299 | $217,956 | $11,783 | | 8,908 |
| Corporate Bonds | 3,480,681 | | 103,873 | 403,578 | 1,057,367 | $1,717,864 | 142,240 | 33,999 | | 414 | | 21,346 |
| Corporate Asset Backed | 959,443 | | 656,144 | 142,133 | 43,677 | 65,621 | | | 15,580 | | | 36,288 |
| Non-U.S. Govt./Sovereign | 1,108,361 | | 441,896 | 595,060 | | | | | | | | 71,405 |
| Short-Term Commercial Paper | 251,101 | | | | | | | | | | $251,101 | |
| Short-Term Agencies | 160,997 | | | | | | | | | | | 160,997 |
| Total Debt Investments | $ 14,358,906 | $4,254,414 | $1,658,963 | $1,235,198 | $1,181,183 | $1,783,485 | $160,305 | $124,298 | $233,536 | $12,197 | $251,101 | $3,464,226 |
| Other Investments | | | | | | | | | | | | |
| U.S. Equity | $ 8,780,486 | | | | | | | | | | | |
| Non-U.S. Equity | 4,179,866 | | | | | | | | | | | |
| Derivatives | 4,264 | | | | | | | | | | | |
| Real Estate | 973,245 | | | | | | | | | | | |
| Private Equities | 26,612 | | | | | | | | | | | |
| Money Market Funds (not rated) | (204) | | | | | | | | | | | |
| Total Other Investments | $ 13,964,269 | | | | | | | | | | | |
| Total Investments | $ 28,323,175 | | | | | | | | | | | |
| Less: Short-term Investments Classified as Cash Equivalent on the Statements of Plan Net Assets | (411,893) | | | | | | | | | | | |
| Total Investments as Shown on Statements of Plan Net Assets | $ 27,911,282 | | | | | | | | | | | |

(1) Includes obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government.

(2) Includes securities that are implicitly guaranteed by the U.S. government but are not rated by Standard and Poor's or Moody's.

(3) A1 is the highest rating category for commercial paper.

(CONTINUED)

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM NOTES TO THE FINANCIAL STATEMENTS JUNE 30, 2011 AND JUNE 30, 2010 (CONTINUED)

**Credit Risk –** Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Credit quality ratings for the TCRS' investments in fixed income securities as of June 30, 2011 and June 30, 2010 are included in the above schedule. Securities are rated using Standard and Poor's and/or Moody's and are presented above using the Standard and Poor's rating scale. The State Pooled Investment Fund has not obtained a credit quality rating from a nationally recognized credit ratings agency.

The TCRS' investment policy specifies that bond issues subject for purchase are investment grade bonds rated in the four highest ratings by one of the recognized rating agencies. In addition, the policy states that private placements that do not have an active secondary market shall be thoroughly researched from a credit standpoint and shall be viewed by TCRS' investment staff as having the credit quality rating equivalent of an AA rating on a publicly traded issue. For short-term investments, the TCRS' investment policy provides for the purchase of only the highest quality debt issues. Commercial paper should be rated in the highest tier by all rating agencies which rate the paper, with a minimum of two ratings required. Commercial paper cannot be purchased if a rating agency has the commercial paper on a negative credit watch. The investment policy also requires preparation of a credit analysis report on the corporation prior to purchasing commercial paper.

As noted above, the TCRS does not utilize its own bank accounts but invests in the State Pooled Investment Fund for its operating cash purposes. Required risk disclosures relative to the State Pooled Investment Fund are presented in the S*tate of Tennessee Treasurer's Report*. That report is available on the state's website at http://www.tn.gov/treasury/.

**Concentration of Credit Risk –** A concentration of investments in any one single issuer of debt securities presents a greater risk for loss in the event that the issuer fails on its obligations. The TCRS had the following investment amounts and percentages of plan net assets, in organizations representing five percent or more of plan net assets, excluding those organizations whose issues are explicitly guaranteed by the United States government, and investments in mutual funds, external investment pools, and other pooled investments:

| | June 30, 2011 | | June 30, 2010 | |
|---|---|---|---|---|
| **Issuer Organization** | **Fair Value** | **Percentage** | **Fair Value** | **Percentage** |
| Federal National Mortgage Association | $2,029,898,227 | 6.03% | $1,989,031,439 | 6.96% |

The TCRS' investment policy limits the maximum amount of a specific corporation's commercial paper that can be purchased to $100 million. There are no specific investment policies that limit investment in any one issuer.

**Interest Rate Risk –** Interest rate risk is the risk that future changes in prevailing market rates of interest will have an adverse effect on the fair value of debt investments. The fair values of securities with long terms to maturity may be highly sensitive to interest rate changes. The TCRS' investment policy does not specifically address limits on investment maturities. The fixed income portfolio, however, is benchmarked against the Citigroup Broad Investment Grade Index and tends to have a duration within a range around that index. Duration is a measure of a debt investment's exposure to fair value changes arising from changing interest rates. It uses the present value of cash flows weighted for those cash flows as a percentage of the investment's full price. The TCRS had the following investments and effective duration at June 30, 2011 and June 30, 2010.

(*CONTINUED*)

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010 (CONTINUED)

**Debt Investments**

*(Expressed in Thousands)*

| Investment Type | Fair Value as of June 30, 2011 | Effective Duration (years) |
|---|---|---|
| Debt Investments | | |
| Government Agencies | $ 397,214 | 5.50 |
| Government Bonds | 1,870,530 | 9.25 |
| Government Inflation Indexed | 2,475,914 | 3.80 |
| Government Mortgage Backed | 3,667,503 | 2.89 |
| Government Asset Backed | 117,625 | 6.31 |
| Municipal Bonds | 149,480 | 10.56 |
| Collateralized Mortgage Obligations (CMO) | 313,391 | 3.82 |
| Commercial Mortgage Backed | 381,608 | 2.21 |
| Corporate Asset Backed Securities | 1,015,712 | 0.71 |
| Corporate Bonds | 3,764,808 | 6.83 |
| Guaranteed Fixed Income | 10,024 | 0.25 |
| Short Term Commercial Paper | 388,064 | 0.01 |
| Total Debt Investments | $14,551,873 | 4.83 |

| Investment Type | Fair Value as of June 30, 2010 | Effective Duration (years) |
|---|---|---|
| Debt Investments | | |
| Government Agencies | $ 526,862 | 5.29 |
| Government Bonds | 2,287,577 | 7.03 |
| Government Inflation Indexed | 2,331,362 | 4.13 |
| Government Mortgage Backed | 3,227,127 | 1.93 |
| Government Asset Backed | 141,172 | 5.75 |
| Municipal Bonds | 118,024 | 9.00 |
| Collateralized Mortgage Obligations (CMO) | 410,479 | 3.44 |
| Commercial Mortgage Backed | 454,043 | 2.31 |
| Corporate Asset Backed Securities | 959,443 | 0.55 |
| Corporate Bonds | 3,480,680 | 5.32 |
| Guaranteed Fixed Income | 10,039 | 0.25 |
| Short Term Commercial Paper | 251,101 | 0.02 |
| Short Term Agencies | 160,997 | 0.02 |
| Total Debt Investments | $14,358,906 | 4.05 |

**Asset-Backed Securities –** The TCRS invests in various collateralized mortgage obligations (CMOs) which are mortgage-backed securities. These securities are based on cash flows from interest and principal payments on underlying mortgages and could therefore be more sensitive to prepayments by mortgagees as a result of a decline in interest rates. The fair value of CMOs at June 30, 2011 was $694,999,254 of which $427,338,919 were CMOs that are generally more sensitive to interest rate changes. The fair value of CMOs at June 30, 2010 was $864,521,465 of which $510,179,228 were CMOs that are generally more sensitive to interest rate changes.

(CONTINUED)

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010 (CONTINUED)

**Foreign Currency Risk –** Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or deposit. The TCRS' investment policy limits the asset allocation for international investments to twenty-five percent of total assets. The TCRS' exposure to foreign currency risk at June 30, 2011 and June 30, 2010 was as follows:

**Foreign Currency-Denominated Investments**
*(Expressed in Thousands)*

| Currency | Total Fair Value June 30, 2011 | Fixed income | Equity | Cash |
|---|---|---|---|---|
| Australian Dollar | $ 284,181 | $ 0 | $ 284,011 | $ 170 |
| British Pound Sterling | 1,042,358 | 67,057 | 975,026 | 275 |
| Canadian Dollar | 1,831,495 | 112,936 | 1,717,840 | 719 |
| Danish Krone | 69,323 | 0 | 69,163 | 160 |
| Euro Currency | 1,397,786 | 99,868 | 1,287,817 | 10,101 |
| Hong Kong Dollar | 134,900 | 0 | 134,886 | 14 |
| Japanese Yen | 1,308,285 | 320,374 | 984,129 | 3,782 |
| New Israeli shekel | 11,348 | 0 | 11,348 | 0 |
| New Zealand Dollar | 4,964 | 0 | 4,945 | 19 |
| Norwegian Krone | 89,807 | 23,985 | 65,639 | 183 |
| Singapore Dollar | 76,919 | 0 | 76,899 | 20 |
| Swedish Krona | 111,190 | 0 | 110,983 | 207 |
| Swiss Franc | 321,680 | 0 | 321,112 | 568 |
| Total | $6,684,236 | $ 624,220 | $6,043,798 | $16,218 |

| Currency | Total Fair Value June 30, 2010 | Fixed income | Equity | Cash |
|---|---|---|---|---|
| Australian Dollar | $ 211,803 | $ 13,958 | $ 195,247 | $ 2,598 |
| British Pound Sterling | 854,109 | 105,779 | 746,819 | 1,511 |
| Canadian Dollar | 377,014 | 118,842 | 257,339 | 833 |
| Danish Krone | 57,646 | 0 | 57,479 | 167 |
| Euro Currency | 1,144,340 | 263,623 | 853,859 | 26,858 |
| Hong Kong Dollar | 116,389 | 0 | 115,557 | 832 |
| Japanese Yen | 1,445,642 | 595,061 | 851,743 | (1,162) |
| New Zealand Dollar | 5,809 | 0 | 5,809 | 0 |
| Norwegian Krone | 56,697 | 11,098 | 45,273 | 326 |
| Singapore Dollar | 58,583 | 0 | 57,470 | 1,113 |
| Swedish Krona | 67,405 | 0 | 67,393 | 12 |
| Swiss Franc | 241,077 | 0 | 240,991 | 86 |
| Total | $4,636,514 | $1,108,361 | $3,494,979 | $33,174 |

(CONTINUED)

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010 (CONTINUED)

**Derivatives –** The TCRS may buy or sell fixed income and equity index futures contracts for the purposes of making asset allocation changes in an efficient and cost effective manner and to improve liquidity. Gains (losses) on futures hedge losses (gains) produced by any deviation from the TCRS' target allocation. The gains and losses resulting from daily fluctuations in the fair value of the outstanding futures contract are settled daily, on the following day, and a receivable or payable is established for any unsettled gain or loss as of the financial statement date. At year end, the TCRS was under contract for fixed income and equity index futures and the resulting payable is reflected in the financial statements at fair value.

The international securities expose the TCRS to potential losses due to a possible rise in the value of the US dollar. The TCRS investment managers can reduce foreign currency exposure by selling foreign currency forward contracts, at agreed terms and for future settlement, usually within a year. The manager will reverse the contract by buying the foreign currency before the settlement date. A gain (loss) on this transaction pair will hedge a loss (gain) on the currency movement of the international security. The TCRS can sell up to 80% of its foreign currency exposure into US dollars. Foreign currency forward contracts expose the TCRS to foreign currency risk as they are denominated in foreign currency. Any unrealized gain on foreign currency forward contracts has been reflected in the financial statements as an investment. The notional amount of the foreign currency forward contracts has been reflected in the financial statements as a receivable and a payable. Any unrealized loss on foreign currency forward contracts has been included in the payable established for the contracts.

The TCRS is authorized to invest in To Be Announced (TBA) mortgage backed securities similar to the foreign currency forward contracts. The TCRS enters into agreements to purchase pools of mortgage backed securities prior to the actual security being identified. The TCRS will roll this agreement prior to settlement date to avoid taking delivery of the security. Any unrealized gain on TBA mortgage backed securities has been reflected in the financial statements as an investment. Any unrealized loss on TBA mortgage backed securities has been included in the payable established for the mortgages. The notional amounts of these agreements have been included in the financial statements as a receivable and a payable. The TCRS invests in these derivatives to adjust its exposure to mortgage coupon risk and to replicate the return on mortgage backed securities portfolios without actually purchasing the security.

The TCRS is authorized to enter into option contracts and any income earned on option contracts has been included in investment income in the financial statements. At year end, the TCRS was under contract for options and the resulting payable is reflected in the financial statements at fair value.

The fair value balances and notional amounts of derivative instruments outstanding at June 30, 2011 and June 30, 2010, classified by type, and the changes in fair value of derivative instrument types for the year ended as reported in the financial statements are as follows:

(*CONTINUED*)

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010 (CONTINUED)

**Derivative Summary**
*(Expressed in Thousands)*

| | Changes in Fair Value | | Fair Value at June 30, 2011 | | | |
|---|---|---|---|---|---|---|
| | Financial Statement Classification | Amount | Financial Statement Classification | Amount | Notional Amount | Currency |
| Foreign Currency Forward Contracts | | $ (121) | | $ (121) | 4,450 | AUD |
| | | (1,304) | | (1,304) | 65,000 | CAD |
| | | (953) | | (953) | 37,260 | EUR |
| | Investment Income | $ (2,378) | Derivative Instruments Payable | $ (2,378) | | |
| Futures Contracts | Investment Income | $ 485,290 | Derivative Instruments Receivable | $ 3,883 | $ 1,585,441 | |
| Options Contracts | Investment Income | $ (17) | Derivative Instruments | $ 11 | $ 11 | |
| TBA Mortgage Backed Ssecurities | Investment Income | $ (767) | Derivative Instruments Payable | $ (767) | $ 260,632 | |

| | Changes in Fair Value | | Fair Value at June 30, 2010 | | | |
|---|---|---|---|---|---|---|
| | Financial Statement Classification | Amount | Financial Statement Classification | Amount | Notional Amount | Currency |
| Foreign Currency Forward Contracts | | $ 2,575 | | $ 2,575 | 99,000 | CAD |
| | | 185 | | 185 | 19,030 | EUR |
| | | 73 | | 73 | 8,270 | GBP |
| | | (536) | | (536) | 6,287,850 | JPY |
| | Investment Income | $ 2,297 | Derivative Instruments | $ 2,297 | | |
| Futures Contracts | Investment Income | $ (23,484) | Derivative Instruments Payable | $ (3,364) | $ 105,747 | |
| TBA Mortgage Backed Ssecurities | Investment Income | $ 1,967 | Derivative Instruments | $ 1,967 | $ 474,634 | |

The fair values of foreign currency forward contracts are estimated based on the present value of their estimated future cash flows. Futures, Options and TBA mortgage backed securities are exchange traded and their price is based on quoted market prices at year end. It is the TCRS policy to conduct derivative transactions through the custodian bank and high quality money center banks or brokerage firms. The credit risk of foreign currency forward contracts is managed by limiting the term of the forward contracts and restricting the trading to high quality banks. The credit risk of futures contracts is managed by maintaining a daily variation margin.

(CONTINUED)

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010 (CONTINUED)

## D. COMMITMENTS

**Standby Commercial Paper Purchase Agreement –** The TCRS has agreed to serve as standby commercial paper purchaser for commercial paper issued by the Funding Board of the State of Tennessee. By serving as a standby commercial paper purchaser, the TCRS receives an annual fee of 60 basis points on the $350 million maximum issuance under this agreement during times when both Moody's and Standard and Poor's investment ratings assigned to the State of Tennessee's general obligation bonds are Aaa and AAA respectively, 80 basis points during times when either Moody's or Standard and Poor's has assigned ratings of Aa and AA respectively, or 105 basis points during times when either Moody's or Standard and Poor's has assigned ratings lower than Aa and AA respectively. In the unlikely event that the TCRS would be called upon to purchase the commercial paper, the TCRS would receive interest at a rate equal to prime plus 75 basis points during the first 30 consecutive days, plus an additional 50 basis points for each consecutive 30 days thereafter, up to a maximum rate allowed by state law.

**Pending Real Estate Items –** At June 30, 2011 the TCRS did not have any commitments for pending real estate purchases. At June 30, 2010 the TCRS had unfunded commitments of $28,500,000 for pending real estate purchases.

**Alternative Investments –** The TCRS had unfunded commitments of $324.1 million and $298.9 million in limited partnerships as of June 30, 2011 and June 30, 2010, respectively.

## E. FUNDED STATUS AND FUNDING PROGRESS

The funded status of each plan as of July 1, 2009, the most recent actuarial valuation date, is as follows (dollar amounts in thousands):

**SCHEDULES OF FUNDING PROGRESS**

*(Expressed in Thousands)*

| | Actuarial Value of Plan Assets (a) | Actuarial Accrued Liability (AAL) Frozen Entry Age (b) | Unfunded AAL (UAAL) (b-a) | Funded Ratio (a/b) | Annual Covered Payroll ( c ) | UAAL as a Percentage of Covered Payroll ((b-a)/c) |
|---|---|---|---|---|---|---|
| **SETHEEPP** | $26,335,199 | $29,054,966 | $2,719,767 | 90.64% | $6,054,528 | 44.92% |
| **PSPP** | $ 5,304,455 | $ 6,143,775 | $ 839,320 | 86.34% | $2,282,082 | 36.78% |

The TCRS uses the Frozen Entry Age actuarial cost method to calculate the annual required contribution (ARC). Effective July 1, 2009, the TCRS reestablished unfunded accrued liabilities for all groups.

The required schedule of funding progress immediately following the notes to the financial statements is intended to present multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

(CONTINUED)

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# NOTES TO THE FINANCIAL STATEMENTS
# JUNE 30, 2011 AND JUNE 30, 2010 (CONTINUED)

Additional information as of the latest actuarial valuation follows:

| | SETHEEPP | PSPP |
|---|---|---|
| Valuation Date | July 1, 2009 | July 1, 2009 |
| Actuarial cost method | Frozen Entry Age | Frozen Entry Age |
| Amortization method | Level Dollar | Level Dollar |
| Remaining amortization period | 20 years closed period | (1) closed period |
| Asset valuation method | 5-year moving market average for FYE on or before June 30, 2007 | 5-year moving market average for FYE on or before June 30, 2007 |
| | 10-year moving market average for FYE after June 30, 2007 | 10-year moving market average for FYE after June 30, 2007 |
| Actuarial assumptions: | | |
| Investment rate of return | 7.50% | 7.50% |
| Projected salary increases | 4.75% (2) | 4.75% (2) |
| Included inflation at | 3.00% | 3.00% |
| Cost-of-living adjustments | 2.50% | 2.50% |
| Increase in Social Security wage base | 3.50% | 3.50% |

(1) An actuarial valuation is performed on each political subdivision participating in the Political Subdivision Pension Plan. Each political subdivision selects the period over which their unfunded accrued liability is amortized, not to exceed 30 years.

(2) Uniform rate that approximates the effect of a graded salary scale.

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# REQUIRED SUPPLEMENTARY INFORMATION
# SCHEDULES OF FUNDING PROGRESS

**SCHEDULES OF FUNDING PROGRESS**
***Expressed in Thousands***

| | Actuarial Valuation Date | Actuarial Value of Plan Assets (a) | Actuarial Accrued Liability (AAL) Frozen Entry Age (b) | Unfunded AAL (UAAL) (b-a) | Funded Ratio (a/b) | Annual Covered Payroll ( c ) | UAAL as a Percentage of Covered Payroll ((b-a)/c) |
|---|---|---|---|---|---|---|---|
| **SETHEEPP** | 7/1/2009 | $26,335,199 | $29,054,966 | $2,719,767 | 90.64% | $6,054,528 | 44.92% |
| | 7/1/2007 | $26,214,995 | $27,240,151 | $1,025,156 | 96.24% | $5,742,866 | 17.85% |
| | 7/1/2005 | $23,627,161 | $23,666,967 | $ 39,806 | 99.83% | $5,245,989 | 0.76% |
| **PSPP** | 7/1/2009 | $ 5,304,455 | $ 6,143,775 | $ 839,320 | 86.34% | $2,282,082 | 36.78% |
| | 7/1/2007 | $ 4,897,974 | $ 5,475,620 | $ 577,646 | 89.45% | $2,081,964 | 27.75% |
| | 7/1/2005 | $ 4,124,013 | $ 4,450,127 | $ 326,114 | 92.67% | $1,890,968 | 17.25% |

The schedule of funding progress is intended to present multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# REQUIRED SUPPLEMENTARY INFORMATION
# SCHEDULES OF EMPLOYER CONTRIBUTIONS

**SCHEDULES OF EMPLOYER CONTRIBUTIONS**
***Expressed in Thousands***

| | SETHEEPP | | PSPP | |
|---|---|---|---|---|
| Year Ended June 30 | Annual Required Contribution | Percentage Contributed | Annual Required Contribution | Percentage Contributed |
| 2011 | $721,759 | 100.00% | $273,781 | 100.00% |
| 2010 | 578,403 | 100.00% | 258,324 | 100.00% |
| 2009 | 583,985 | 100.00% | 252,926 | 100.00% |
| 2008 | 593,412 | 100.00% | 244,847 | 100.00% |
| 2007 | 562,729 | 100.00% | 231,699 | 100.00% |
| 2006 | 474,879 | 100.00% | 191,000 | 100.00% |

An actuarial valuation of the TCRS is performed every two years with the next valuation scheduled to be effective July 1, 2011.

# TENNESSEE CONSOLIDATED RETIREMENT SYSTEM
# ACTUARIAL BALANCE SHEET

**ACTUARIAL BALANCE SHEET**
***as of July 1, 2009***

| | State Employees, Teachers, Higher Ed. Employees Pension Plan (SETHEEPP) | Political Subdivision Pension Plan (PSPP) | Total |
|---|---|---|---|
| ASSETS | | | |
| Present assets creditable to | | | |
| Employer accumulation fund | $22,775,436,290 | $ 4,293,104,552 | $ 27,068,540,842 |
| Members' accumulation fund | 3,559,762,929 | 1,011,350,909 | 4,571,113,838 |
| Total present assets | 26,335,199,219 | 5,304,455,461 | 31,639,654,680 |
| Present value of prospective contributions payable to: | | | |
| Employer accumulation fund | | | |
| Normal | 3,975,132,757 | 1,312,768,669 | 5,287,901,426 |
| Accrued liability | 2,719,767,478 | 839,320,076 | 3,559,087,554 |
| Total employer accumulation | 6,694,900,235 | 2,152,088,745 | 8,846,988,980 |
| Member's accumulation fund | 1,754,226,527 | 569,888,332 | 2,324,114,859 |
| Total prospective contributions | 8,449,126,762 | 2,721,977,077 | 11,171,103,839 |
| TOTAL ASSETS | $34,784,325,981 | $ 8,026,432,538 | $ 42,810,758,519 |
| LIABILITIES | | | |
| Present value of prospective benefits payable on account of: | | | |
| Present retired members and beneficiaries | $14,122,766,225 | $ 2,190,077,255 | $ 16,312,843,480 |
| Present active members | 20,002,441,459 | 5,624,931,055 | 25,627,372,514 |
| Former members | 659,118,297 | 211,424,228 | 870,542,525 |
| TOTAL LIABILITIES | $34,784,325,981 | $ 8,026,432,538 | $ 42,810,758,519 |