STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD

Financial Statements as of and for the Years Ended June 30, 2009 and 2008, and Independent Auditors' Report

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STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD

Financial Statements
and Other Supplementary Information
June 30, 2009 and 2008

(With Independent Auditors' Report Thereon)

Prepared By Board Staff

AUDITED BY:
MOSS ADAMS LLP

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EDUCATIONAL RETIREMENT BOARD

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STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD

Official Roster
As of June 30, 2009

BOARD OF DIRECTORS

NAME	TITLE
Mr. Bruce Malott	Chairman
Ms. Mary Lou Cameron	Vice-Chairman
Mr. Gary Bland	Secretary
Dr. Beulah Woodfin	Member
Mr. H. Russell Goff	Member
Dr. Veronica Garcia	Ex-officio Member
Mr. James B. Lewis	Ex-officio Member

ADMINISTRATIVE STAFF

Ms. Jan Goodwin	Executive Director
Mr. Jeffrey M. Riggs	Deputy Director
Mr. Chris Schatzman	General Counsel
Mr. Bob Jacksha	Chief Investment Officer
Mr. Robert K. Westervelt	Chief Financial Officer
Ms. Clara Mares	Administrative Services Manager
Mr. Greg Trujillo	Information Technology Manager
Mr. Steve Moreno	Member Services Manager
Vacant	Outreach/Branch Offices

FINANCIAL SECTION

Independent Auditors' Report

To the Members of the State of New Mexico
Educational Retirement Board
and
Mr. Hector H. Balderas
New Mexico State Auditor

We have audited the accompanying Statements of Plan Net Assets and Statements of Changes in Plan Net Assets of the State of New Mexico Educational Retirement Board (the "ERB"), as of and for the years ended June 30, 2009 and 2008, as listed in the table of contents. We have also audited the Schedule of Revenues and Expenses – Budget and Actual (Non-GAAP Basis) shown as supplemental information for the year ended June 30, 2009, as listed in the table of contents. These financial statements and schedule are the responsibility of ERB'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 with the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the ERB's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 opinions.

As discussed in Note 1, the financial statements of ERB are intended to present the net assets and changes in net assets of only that portion of the State of New Mexico which are attributable to the transactions of the Fund administered by ERB. They do not purport to, and do not present fairly, the financial position of the State of New Mexico as of June 30, 2009 and 2008, 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.

To the Members of the State of New Mexico
Educational Retirement Board
and
Mr. Hector H. Balderas
New Mexico State Auditor

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the plan net assets of ERB as of June 30, 2009 and 2008, and the respective changes in plan net assets for the year then ended in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the Schedule of Revenues and Expenses - Budget and Actual, (Non-GAAP Basis) presents fairly the revenues and expenses on the basis of accounting as described in Note 2, for the year ended June 30, 2009.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 4, 2009, on our consideration of the ERB's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis on pages 8 to 15 and Required Supplementary Schedules of Funding Progress and of Employer Contributions on pages 48 to 50 are not a required part of the 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 audit was conducted for the purpose of forming opinions on the financial statements of ERB taken as a whole. The Schedule of Cash Accounts, as listed in the table of contents, is presented for purposes of additional analysis and is not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

The Schedule of Accountability in Government Act – Performance Measures, as listed as supplemental information in the table of contents, is presented for purposes of additional analysis and is not a required part of the financial statements.

Moss Adams LLP

Albuquerque, New Mexico
December 4, 2009

Agency management prepared this Management's Discussion and Analysis ("MD&A") of the financial position of the State of New Mexico Educational Retirement Board ("Board") for the fiscal years ended June 30, 2009 ("FY09"), 2008 ("FY08"), and 2007 ("FY07"). For more detailed information of the Board's FY09 and FY08 financial activities, the reader should review the financial statements, including the notes and required supplementary information.

FINANCIAL REPORTING REQUIREMENTS

The financial statements include the Statements of Plan Net Assets and the Statements of Changes in Plan Net Assets. The financial statements also include notes, which explain the history and purpose of the Board, significant accounting policies, investment details, statutory disclosures, and other required supplementary information. These financial statements have been prepared in accordance with generally accepted accounting principles as promulgated by the Governmental Accounting Standards Board ("GASB").

FINANCIAL HIGHLIGHTS

- Net assets held in trust for pension benefits decreased $1.7 billion, or 18.9%, in FY09 compared to a decrease of $686 million, or 7.25%, in FY08 and an increase of $1.2 billion, or 15%, in FY07. The primary driver was a notable downward trend in both domestic and foreign financial markets beginning at the end of FY08.

- Investment advisor fees and custodial fees decreased $3.6 million, or 17.8%, in FY09 compared to a decrease of $0.5 million, or 2.1% in FY08 and an increase of $3.7 million, or 22%, in FY07. Higher fees incurred with an expanding portfolio in alternative investments were offset by the decrease in assets under management discussed above.

- Total cash and cash equivalents decreased $44 million in FY09 compared to a $23 million increase in FY08 and an $88 million increase in FY07. As the board had been adjusting holdings in the weak markets at the end of FY08 cash balances increased, but as financial markets strengthened toward the end of FY09 more of that cash had been returned to active investment. Total cash and cash equivalents equaled $307 million, or 4.1% of investments, at the end of FY09 compared to $351 million, or 3.7% of investments, at the end of FY08, and $327 million, or 3.2% of investments at the end of FY07. All three years were within the Board's investment policy that limits cash holdings to 5% or less. The higher relative percentage of cash to total investment assets at the end of FY09 is reflective of the overall decrease in portfolio value.

- Investment holdings decreased $2.05 billion, or 21.4%, in FY09 compared to a decrease of $723 million, or 7.0%, in FY08 and an increase of $1.4 billion, or 15.2% in FY07, primarily due to the weak performance of domestic and foreign equity markets at the end of FY08 and continuing through FY09.

- Receivables decreased by just under $161 million in FY09 compared to a decrease of $594 million in FY08, and an increase of $876 million in FY07, with the majority of the changes showing in investment broker sales proceeds. A decrease indicates a smaller volume of investments were sold at or near fiscal year end, and remained outstanding on June 30, while the increase in FY07 indicates a larger volume was sold at year end that year. Securities sales and purchases are usually based on "trade date + 3 days," meaning that the transaction will settle three business days after it is initiated.

- Capital assets decreased by $1.9 million, or 18.7%, in FY09 compared to an increase of $2.6 million, or 34.4%, in FY08 and an increase in FY07 of $100 thousand, or 1.3%. The big increase in FY08 was due primarily to capitalization of development costs on the new pension administration system and the addition to the Santa Fe office building. The big decrease in FY09 was mainly the result of large depreciation costs, mostly on the pension administration system capitalized last year with a relatively short depreciation period, combined with minimal new asset additions during the year. See notes two and seven for additional information on capital asset activity and depreciable life expectancies. The Board does not have any debt activity.

- Accounts payable decreased $1.3 million, or 24.1%, in FY09 compared to an increase of $537 thousand, or 10.8%, in FY08 and an increase of $103 thousand, or 2.11% in FY07, primarily due to a decrease in the amount of investment advisor fees due at FY09 year-end.

- Investment purchases payable-brokers decreased by $143 million in FY09 compared to a decrease of $419 million in FY08 and an increase of $636 million in FY07. A decrease is indicating that a smaller volume of investments were purchased at or near fiscal year end and remained outstanding on June 30, while the increase in FY07 indicates a larger volume was purchased at year end that year. Securities sales and purchases are usually based on "trade date + 3 days," meaning that the transaction will settle three business days after it is initiated.

- Securities lending collateral decreased $458 million, or 40.3%, in FY09 compared to a decrease of $199 million, or 15.1%, in FY08, and an increase of $451 million, or 51.9% in FY07. This indicates a smaller amount from the Board's portfolio was being lent at the end of FY09 and FY08. Securities lending net income decreased $1.1 million, or 18.6%, in FY09 compared to an increase of $3.5 million, or 152%, in FY08 and an increase of $182 thousand, or 8.5%, in FY07. The decrease from FY08 to FY09 was due to a significant drop in interest rates. The increase from FY07 to FY08 was due to lower "borrower rebates" paid on the lent securities.

- Employer and member contributions increased $42.9 million, or 8.7%, in FY09 compared to an increase of $47.5 million, or 10.7%, in FY08 and an increase of $40.5 million, or 10.0% in FY07, due to an increase in active member contribution rates and salary increases. Benefit payments to retirees increased $38.9 million, or 6.7%, in FY09 compared to an increase of $38.6 million, or 7.15%, in FY08 and an increase of $46 million, or 9.3% in FY07, due to the increase in the number of retirees each year, as well as the cost of living adjustments paid to retirees. Refunds and interest to terminated members increased $211 thousand, or 0.7%, in FY09 compared to an increase of $1.9 million, or 7.1%, in FY08 and a decrease of $0.8 million, or 2.8% in FY07. The Board's total membership increased by 2,023, or 1.6%, to 126,895 members in FY09 compared to an increase of 2,274, or 1.8%, to 124,872 members in FY08 and an increase of 2280, or 1.9%, to 122,598 members in FY07.

CONDENSED FINANCIAL INFORMATION

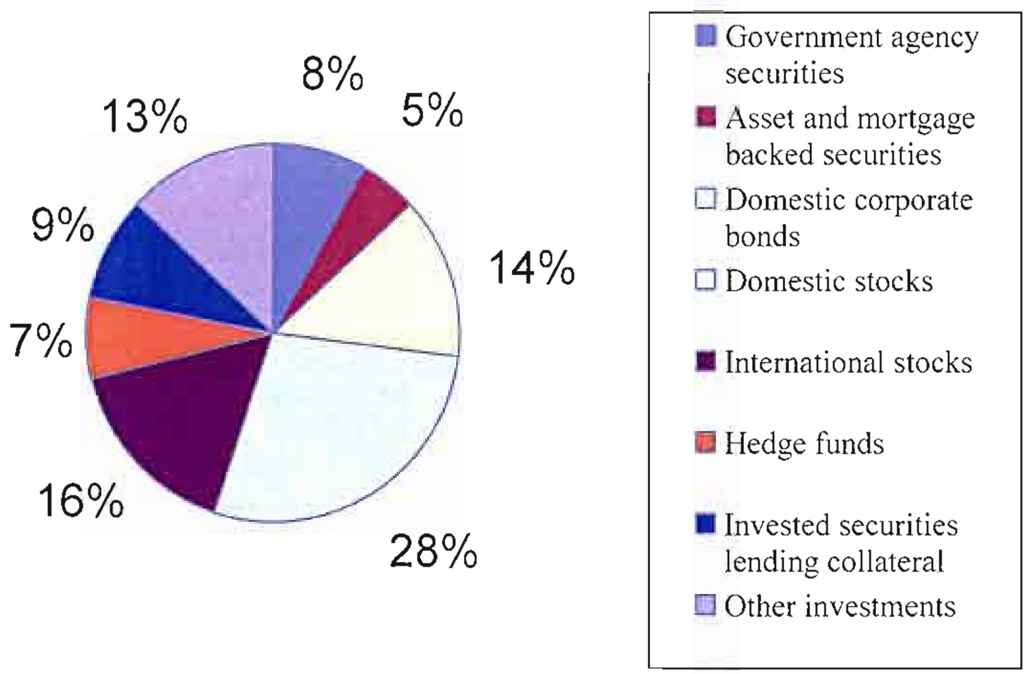
Statements of Plan Net Assets

	FY09	FY08	FY07
Cash and short-term investments	$ 289,479,681	$ 346,040,280	$ 316,614,628
Receivables	223,723,966	384,628,705	978,651,452
Investment in State General Fund Investment Pool	17,627,763	4,990,356	11,124,535
Investments—at fair value	7,523,202,286	9,575,761,825	10,298,665,645
Capital assets (net of accumulated depreciation)	8,226,741	10,121,468	7,528,949
Total assets	8,062,260,437	10,321,542,634	11,612,585,209
Current liabilities	948,409,876	1,551,286,681	2,156,597,869
Long-term liabilities (compensated absences)	198,861	211,914	191,487
Total liabilities	948,608,737	1,551,498,595	2,156,789,356
Net assets held in trust for pension benefits	$7,113,651,700	$8,770,044,039	$9,455,795,853

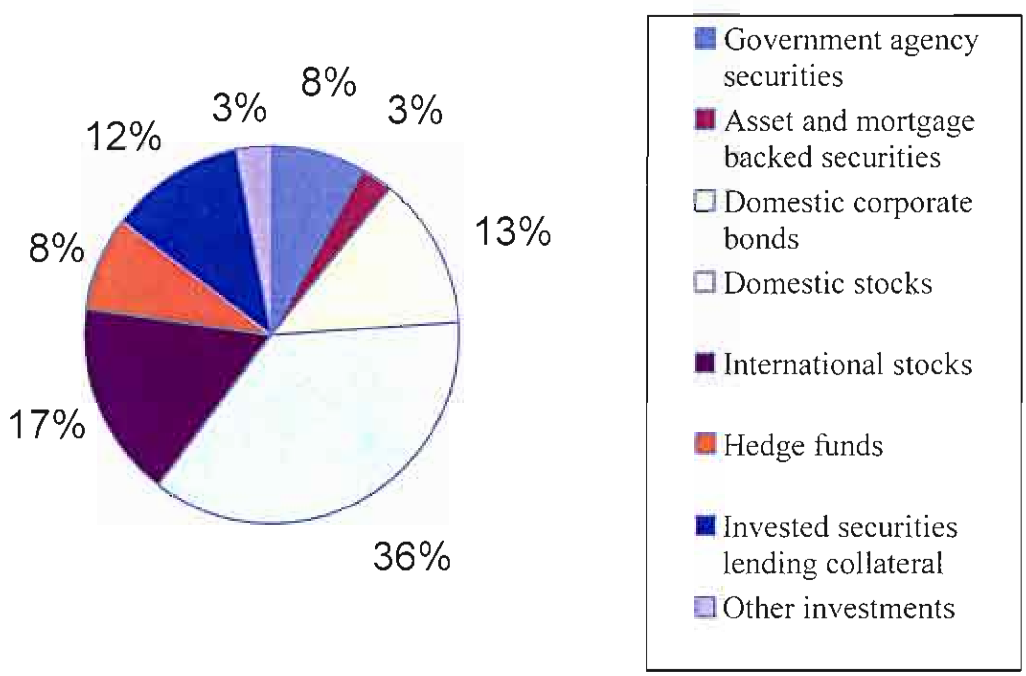
Statements of Changes in Plan Net Assets

	FY09	FY08	FY07
Contributions	$ 535,699,520	$ 492,762,295	$ 445,244,346
Investment income less investment expenses	185,177,492	217,647,920	182,784,302
Net (depreciation) appreciation in the fair value of investments	(1,724,901,896)	(785,485,191)	1,177,439,939
Other income	3,696,085	3,662,453	4,331,489
Total (deductions) additions	(1,000,328,799)	(71,412,523)	1,809,800,076
Benefit payments	617,705,038	578,775,611	540,143,723
Refunds	29,686,510	29,475,171	27,525,131
Administrative expenses	8,671,992	6,088,509	5,625,343
Total deductions	656,063,540	614,339,291	573,294,197
(Decrease) Increase in net assets	(1,656,392,339)	(685,751,814)	1,236,505,879
Net assets held in trust for pension benefits:			
Beginning of year	8,770,044,039	9,455,795,853	8,219,289,974
End of year	$7,113,651,700	$8,770,044,039	$9,455,795,853

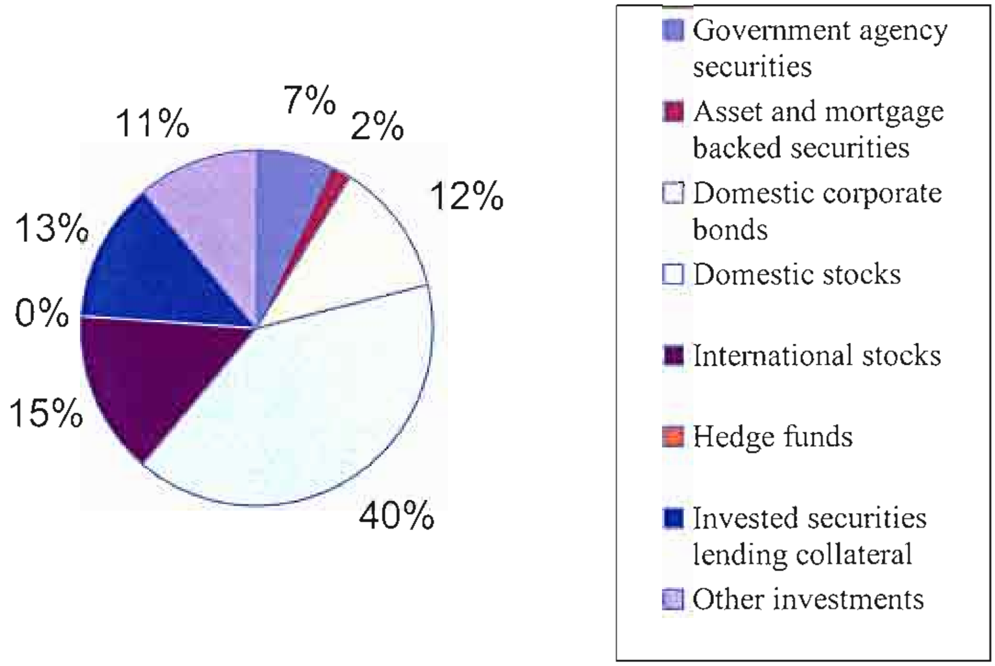
FY09 Investments by Category



FY08 Investments by Category



FY07 Investments by Category



BUDGETARY HIGHLIGHTS

A major portion of the Board's contractual services are based on market performance, and the budget is established to absorb all expenses that may be incurred during the period. These initial budget estimates may be adjusted throughout the year, based on market performance, to arrive at a final budget. In FY09, the Board's initial budget was increased by $530 thousand from $32.4 million to $32.9 million. In FY08 the budget was not changed from the original $30.1 million. In FY07 the budget was increased by $2.7 million from $29.5 million to $32.2 million. Changes in the corpus of the fund generally drive changes in income and expenses. More assets under management combined with better performance will result in increased income and associated management fees and other expenses. In fiscal years like 2009 and 2008, with decreasing asset balances, income and associated management fees and other expenses will generally decrease. The Board had savings over budgeted amounts totaling $7.5 million in the three expense categories during the 2009 fiscal year compared to a savings of $3.8 million in 2008 and savings of $6.6 million in fiscal year 2007.

LONG-TERM DEBT

The only long-term liability activity relates to compensated absences reported in Note 9.

INFRASTRUCTURE

ERB has no infrastructure assets to report.

CAPITAL ASSETS

The Net Investment in Capital Assets at June 30, 2009, 2008 and 2007, is as follows:

Description	Cost	Accumulated Depreciation	Book Value
2009			
Land	$ 248,172	$ -	248,172
Depreciable land improvements	19,361	(3,111)	16,250
Capital assets in progress	-	-	-
Integrated Retirement Information System	9,156,963	(3,786,081)	5,370,882
Building and building improvements	3,365,714	(1,126,826)	2,238,888
Furniture and equipment	1,139,019	(786,470)	352,549
Total	$ 13,929,229	$ (5,702,488)	$ 8,226,741
2008			
Land	$ 248,172	$ -	$ 248,172
Depreciable land improvements	19,361	(2,412)	16,949
Capital assets in progress	1,176,211	-	1,176,211
Integrated Retirement Information System	9,156,963	(1,954,689)	7,202,274
Building and building improvements	2,151,067	(1,011,482)	1,139,585
Furniture and equipment	1,078,738	(740,461)	338,277
Total	$ 13,830,512	$ (3,709,044)	$ 10,121,468
2007			
Land	$ 248,172	$ -	$ 248,172
Depreciable land improvements	1,875	(1,688)	187
Capital assets in progress	-	-	-
Integrated Retirement Information System	6,396,673	(629,350)	5,767,323
Building and building improvements	2,151,067	(846,467)	1,304,600
Furniture and equipment	1,087,812	(879,145)	208,667
Total	$ 9,885,599	$ (2,356,650)	$ 7,528,949

CURRENTLY KNOWN FACTS AND CONDITIONS

The accompanying financial statements reflect a significant decline in the reported values of ERB's investment portfolio beginning in FY08 and continuing into FY09. However, because the values of individual investments fluctuate with market conditions, the amount of losses or gains that ERB will recognize in our future financial statements cannot be determined. Subsequent to June 30, 2009, investment markets have generally been positive but continue to be volatile.

ERB has invested the cash collateral from securities in low-risk conservative investment vehicles such as commercial paper, repurchase agreements, cash equivalents, domestic corporate bonds, and asset backed securities. With the financial markets being extremely volatile and with the possibility of significant declines in values of financial instruments occurring, ERB potentially could have a loss on these collateral investments resulting in ERB liquidating assets to offset the loss. However, ERB believes that it has largely mitigated this risk through its investment strategy for these assets.

FINANCIAL CONTACT

Any questions regarding the financial statements of ERB should be directed to the ERB Chief Financial Officer at (505) 476-6132 or by mail at 701 Camino de los Marquez Santa Fe, New Mexico 87505

STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD
STATEMENTS OF PLAN NET ASSETS
June 30, 2009 and 2008

	2009	2008
Assets		
Cash	$ 907	$ 4,751
Short term investments	289,478,774	346,035,529
Receivables		
Contributions	66,650,037	66,582,666
Investment sales proceeds-brokers	129,477,330	286,904,399
Interest and dividends	27,528,119	31,018,123
Other	68,480	123,517
Total receivables	223,723,966	384,628,705
Interest in State General Fund Investment Pool	17,627,763	4,990,356
Investments, at fair value		
U. S. Treasury securities	230,027,482	166,650,949
Government agency securities	614,167,396	764,776,546
Asset and mortgage backed securities	350,555,573	280,538,993
Domestic corporate bonds	1,044,370,430	1,257,449,902
Domestic stocks	2,080,792,320	3,546,803,558
International stocks	1,238,816,417	1,583,681,765
Private equity	138,357,638	93,682,458
Hedge funds	537,791,270	722,726,369
Private real estate	77,902,570	34,450,129
Other investments	545,166,380	2,564,355
Invested securities lending collateral	665,254,810	1,122,436,801
Total investments	7,523,202,286	9,575,761,825
Capital assets, at cost, net of accumulated depreciation of $5,702,488 and $3,709,044 respectively	8,226,741	8,945,257
Capital assets in progress	-	1,176,211
Total capital assets	8,226,741	10,121,468
Total assets	$ 8,062,260,437	$ 10,321,542,634
Liabilities		
Accounts payable	$ 4,167,084	$ 5,490,449
Accounts payable school contributions	101,310	65,780
Accrued payroll and employee benefits	154,292	150,596
Accrued compensated absences	198,861	211,914
Refunds payable	943,130	1,684,509
Investment purchases payable	263,999,480	407,395,504
Funds held for others	850,156	136,133
Securities lending collateral	678,194,424	1,136,363,710
Total liabilities	948,608,737	1,551,498,595
Net assets held in trust for pension benefits	$ 7,113,651,700	$ 8,770,044,039

See Accompanying Notes to Financial Statements.

STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD
STATEMENTS OF CHANGES IN PLAN NET ASSETS
Years Ended June 30, 2009 and 2008

	2009	2008
Additions		
Contributions		
Employer	$ 323,685,497	$ 290,846,065
Member	212,014,023	201,916,230
Total contributions	535,699,520	492,762,295
Investment income from investing activities		
Net change in fair value of investments	(1,724,901,896)	(785,485,191)
Interest income	114,363,735	158,600,235
Dividend income	82,815,387	73,576,472
Total investing activity (loss)	(1,527,722,774)	(553,308,484)
Investing activity expenses:		
Investment advisor fees	(16,103,831)	(19,700,796)
Custody fees	(670,671)	(692,531)
Total investing activity expenses	(16,774,502)	(20,393,327)
Net loss from investing activities	(1,544,497,276)	(573,701,811)
From securities lending activities		
Securities lending income	19,017,334	64,146,240
Securities lending expenses:		
Borrower rebates	(13,564,740)	(57,443,914)
Agent fees	(679,722)	(837,786)
Total securities lending expenses	(14,244,462)	(58,281,700)
Net income from securities lending activities	4,772,872	5,864,540
Total net investment loss	(1,539,724,404)	(567,837,271)
Miscellaneous income		
Penalties	3,568	22,072
Interest on restoration of service	3,093,720	3,443,975
Other	598,797	196,406
Total miscellaneous income	3,696,085	3,662,453
Total (decrease) additions	(1,000,328,799)	(71,412,523)
Deductions		
Refunds to terminated members	24,051,878	23,729,865
Interest on refunds	5,634,632	5,745,306
Administrative expenses	8,671,992	6,088,509
Age and service benefit payments	610,664,369	572,191,714
Disability benefit payments	7,040,669	6,583,897
Total deductions	656,063,540	614,339,291
Net decrease	(1,656,392,339)	(685,751,814)
Net assets held in trust for pension benefits		
Beginning of the year	8,770,044,039	9,455,795,853
End of the year	$ 7,113,651,700	$ 8,770,044,039

See Accompanying Notes to Financial Statements.

NOTE 1. EDUCATIONAL RETIREMENT BOARD

Plan Description—The State of New Mexico Educational Retirement Board ("Board") was created by the Educational Retirement Act, Section 22-11-1 through 22-11-52, NMSA 1978, as amended, to administer and have the responsibility for operating the Educational Employees' Retirement Plan (the "Plan"). The Plan is a cost-sharing, multiple-employer plan established and administered by the Board to provide retirement, disability, and death benefits for all certified teachers and other employees of the State of New Mexico (the "State") educational institutions, junior colleges, and technical-vocational institutions.

Contributing employers to the Plan include the following:

Public schools	89
Universities and colleges	15
Charter schools	67
Special schools	4
State agencies	11
	186

Reporting Entity—The Board is an agency of the State. The Plan administered by the Board is considered part of the State financial reporting entity and is a pension trust fund of the State.

The Board has developed criteria to determine whether other state agencies, boards, or commissions that benefit the members of the Board should be included within its financial reporting entity as component units. The criteria include, but are not limited to, whether the Board exercises oversight responsibility; financial interdependency; selection of governing authority; designation of management; ability to significantly influence operations; and accountability for fiscal matters, scope of public service, and special financing relationships. Based on these criteria, management of the Board has determined that there are no component units that should be included in its financial reporting entity.

Participation—Membership in the Plan is a condition of employment. Employees of public schools, universities, colleges, junior colleges, technical-vocational institutions, state special schools, charter schools, and state agencies providing an educational program, who are employed more than 25% of a full-time equivalency, are required to be members of the Plan.

The Board serves 186 employers in the State and has an active and inactive membership of 126,895 and 124,872 in 2009 and 2008, respectively. The status and number of all participants at June 30, 2009 and 2008 consisted of the following:

	2009	2008
(1) Retirees and beneficiaries of deceased retirees currently receiving benefits	32,497	31,192
(2) Inactive members	30,576	29,982
(3) Current active members	63,822	63,698
	126,895	124,872

NOTE 1. EDUCATIONAL RETIREMENT BOARD (CONTINUED)

Benefit Provisions - A member's retirement benefit is determined by a formula which includes three component parts: the member's final average salary ("FAS"), the number of years of service credit, and a 0.0235 constant factor. The FAS is the average of the member's salaries for the last five years of service or any other consecutive five-year period, whichever is greater.

A brief summary of Plan coverage provisions follows:

For members employed before July 1, 2009, a member is eligible to retire when one of the following events occurs:

- The member's age and earned service credit add up to the sum of 75 or more.
- The member is at least sixty-five years of age and has five or more years of earned service credit.
- The member has service credit totaling 25 years or more.

Chapter 288, Laws of 2009 changed the eligibility requirements for new members first employed after July 1, 2010. The eligibility for a member who either becomes a new member on or after July 1, 2010, or at any time prior to that date refunded all member contributions and then becomes reemployed after that date is as follows:

- The member's age and earned service credit add up to the sum of 80 or more.
- The member is at least sixty-seven years of age and has five or more years of earned service credit.
- The member has service credit totaling 30 years or more.

(1) A further requirement to be eligible to retire is that a member must have at least one year of employment after July 1, 1957, and at least five years of contributory employment. Eligible members who have one year of employment after July 1, 1957, but less than the required five years of contributory employment, may contribute to the fund for each year needed. The cost of such contributions is a sum equal to the prevailing combined contributions of the member and the local administrative unit in effect at the time the contributory employment is acquired, which was 19.55% as of June 30, 2009, times the average annual salary of the last five years, for each year of contributory employment needed, plus 3% compounded interest from July 1, 1957, to the date of payment.

(2) *Forms of Payment* - The benefit is paid as a monthly life annuity with a guarantee that, if the payments made do not exceed the member's accumulated contributions, determined as of the date of retirement, the balance will be paid in a lump sum to the member's surviving beneficiary.

(3) *Normal Benefit* - There are no reductions to the monthly benefit, and there is no continuing benefit due to a beneficiary or estate, except the balance, if any, of contributions less benefits paid.

NOTE 1. EDUCATIONAL RETIREMENT BOARD (CONTINUED)

(4) *Optional Forms of Payment* - There are two optional forms of payment available: Option B or Option C. The benefit reduction with an Option B or C form of payment depends on the age of the member and the age of the beneficiary at the time of retirement. The form of payment election and the beneficiary designated to receive a survivor's benefit are irrevocable. Details of Options B and C are as follows:

Option B - The normal monthly benefit is reduced to provide for a 100% survivor's benefit. The reduced benefit is payable during the life of the member, with the provision that, upon death, the same benefit is paid to the beneficiary for his or her lifetime. The named beneficiary may not be changed after the effective date of retirement. If the beneficiary predeceases the member, the member's benefit is adjusted by adding back the amount by which the benefit was reduced at retirement due to the election of Option B retroactively to the time of retirement.

Option C - The normal monthly benefit is reduced to provide for a 50% survivor's benefit. The reduced benefit is payable during the life of the member, with the provision that, upon death, the reduced 50% benefit is paid to the beneficiary for his or her lifetime. The named beneficiary may not be changed after the effective date of retirement. If the beneficiary predeceases the member, the member's benefit is adjusted by adding the amount by which the benefit was reduced at retirement due to the election of Option C retroactively to the time of retirement.

(5) *Cost of Living Adjustment* - Retired members and surviving beneficiaries receiving benefits receive an automatic cost of living adjustment ("COLA") to their benefit each July 1, beginning in the year the member attains or would have attained age 65 or on July 1 of the year following the member's retirement date, whichever is later. The adjustment is equal to one-half the change in the Consumer Price Index ("CPI"), except that the COLA shall not exceed 4% nor be less than 2%, unless the change in CPI is less than 2%, in which case, the COLA would equal the change in CPI. Members retired prior to July 1, 1984, are also entitled to an increase of the lesser of 3% or the increase in CPI for years prior to the attainment of age 65.

Members on disability retirement are entitled to a COLA commencing on July 1 of the third full year following disability retirement. A member on regular retirement who can prove retirement because of a disability may qualify for a COLA beginning July 1 in the third full year of retirement.

NOTE 1. EDUCATIONAL RETIREMENT BOARD (CONTINUED)

(6) *Disability Retirement*:

Eligibility - A member is eligible for a disability benefit provided (a) he or she has credit for at least 10 years of service, and (b) the disability is approved by the Board.

Monthly Benefit - The monthly benefit is equal to 2% of FAS times years of service, but not less than the smaller of (a) one-third of FAS or (b) 2% of FAS times years of service projected to age 60.

Form of Payment - The disability benefit commences immediately upon the member's retirement. Disability benefits are payable as a monthly life annuity, with a guarantee that, if the payments made do not exceed the member's accumulated contributions, determined as of the date of retirement, the balance will be paid in a lump sum to the member's surviving beneficiary. If the disabled member survives to age 60, the regular optional forms of payment are available.

(7) *Deferred Retirement* - A member with five or more years of earned service credit on deferred status may retire when eligible under the Rule of 75 or when the member attains age 65.

(8) The Educational Retirement Act, Section 22-11-1 to 22-11-53, NMSA 1978, assigns the authority to establish and amend benefit provisions to the Board.

Refund of Contributions - Members may withdraw their contributions only when they terminate covered employment in the State and certification of termination has been provided by their former employers. Interest paid to members when they withdraw their contributions following termination of employment is at a rate set by the Board. Interest is not earned on contributions credited to accounts prior to July 1, 1971, or those on deposit for less than one year.

Alternative Retirement Plan - The New Mexico legislature established the Alternative Retirement Plan ("ARP") through the enactment of NMSA 1978, Sections 22-11- 47 through 52. In contrast to the regular defined benefit plan administered by the Educational Retirement Board ("ERB"), the ARP is a defined contribution plan. Beginning on July 1, 1991 at the State's six institutions of higher education, and July 1, 1999 at the State's eight community colleges (the colleges and universities are referred to as the "qualifying state educational institutions"), certain faculty and professional employees in eligible positions have the option of electing to participate in the ARP in lieu of participating in the regular defined benefit plan. Information about the ARP is provided to eligible employees by their employers. Employees must make the election to participate in the ARP within 90 days of employment; those who do not elect to participate in the plan become members of the regular defined benefit plan. Pursuant to statute, ARP retirement benefits may be only in the form of a lifetime annuity, except in the case of death, when single sum cash payments are allowed.

NOTE 1. EDUCATIONAL RETIREMENT BOARD (CONTINUED)

Two carriers have been approved to offer annuities to the participants: Teachers Insurance and Annuity Association/College Retirement Equities Fund ("TIAA-CREF"), and Variable Annuity Life Insurance Company ("VALIC" or "AIG VALIC," now known as "AIG Retirement"). Employees are allowed to transfer between carriers once each year.

For the year ended June 30, 2009, employees under the ARP contribute 7.90% of their gross salaries. The colleges and universities are required to contribute 8.65% to the carrier on behalf of the participant and 3% to the regular defined benefit plan to help fund the unfunded accrued actuarial liability. The 3% fee remitted to ERB for the years ended June 30, 2009, 2008 and 2007 was $4,726,836, $4,469,033, and $3,806,933, respectively.

The 3% fee does not provide retirement benefits. The colleges and universities are responsible for submitting the employers' and the employees' contributions directly to the annuity carriers. Vesting is immediate for all contributions.

As noted above, the ARP is a defined contribution plan; benefits are determined strictly by contributions made and earnings on contributions. Participating employees are responsible for, and accept the risks of, selecting investments from those offered by the carriers and for managing their investments. Retirement benefits are computed and paid by the annuity carriers; the ERB does not compute or pay the retirement benefits. If a participant seeks to retire due to disability, the annuity carrier determines the disability and computes the lifetime annuity.

Chapter 9 Laws of 2009 established certain changes to the Alternative Retirement Plan, including authorizing additional carriers, allowing plan members to take withdrawals for rollover to other qualified plans, and allowing a one time option for members with seven years of contributory service to switch to the defined benefit plan going forward, but the member's previous contributions to the ARP plan remain in that plan and the five year service requirement and benefit calculation in the regular ERB Defined Benefit plan are effective as of the first day of the month following the month in which a valid election to switch is made.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting—The Board's financial statements are prepared using the economic resource measurement focus and the accrual basis of accounting. The General Appropriation Act establishes the modified accrual basis of accounting for governmental funds as the budgetary basis for the State. Prior-year encumbrances are not carried forward for single-year appropriations. Employer and member contributions are recognized as revenue in the period in which the member's services are performed. Benefits and refunds are recognized when due and payable in accordance with the terms of the Plan.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Budgets and Budgetary Accounting—Formal budgetary integration is used as a management control device by the Board in administering the Plan. The budget for this State Agency is adopted on the modified accrual basis of accounting, except for accounts payable accrued at the end of the fiscal year that do not get paid by the statutory deadline (Section 10-6-4 NMSA 1978), that must be paid out of the next year's budget.

Only administrative expenses and a small portion of interest income are budgeted, while significant revenues and non-administrative expenses are not. The budget is prepared on a non-GAAP basis, as it recognizes encumbrances and capital expenses as current expenses, excludes depreciation expense, and recognizes revenue when cash is received. Budgetary comparisons for the Plan are presented in the schedule of revenues and expenses—budget and actual (non-GAAP basis).

The Accountability in Government Act, Chapter 15, Laws of 1999, provides a general process for implementation of performance-based budgeting over a four-year period. The Board was included in performance-based budgeting for the first time in FY 2002. The Board developed performance measures, which were approved by the State Budget Division ("SBD") and the Legislative Finance Committee ("LFC") and included in the General Appropriations Act. The Board is required to periodically report to the SBD and the LFC on these performance measures.

The original budget was amended during the fiscal year. A single Budget Adjustment Request (BAR) was submitted and approved for the addition of $530 thousand in the contractual services expense item. The additional expense was approved to be funded from existing Fund Balance.

The Board follows these procedures in establishing the annual budget:

(1) By August 31, the Board prepares a Budget Appropriation Request to be presented to the next legislature. The Request includes proposed expenses and the means of financing them.

(2) On September 1, the Budget Appropriation Request is submitted to the Department of Finance and Administration ("DFA") and the LFC.

(3) The DFA makes recommendations and adjustments to the Board's Budget Appropriation Request, which becomes the Governor's proposal to the Legislature.

(4) The LFC holds hearings on the Budget Appropriation Request. Recommendations and adjustments are made prior to presenting the Budget Appropriation Request to the Legislature.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(5) Both the DFA's and the LFC's recommended appropriation proposals are presented to the Legislature for approval of the final budget.

(6) On May 1, the Board submits its Annual Operating Budget to the DFA and the LFC based on the final appropriation from the Legislature.

(7) Budgetary control is exercised at the appropriation unit level (revenue source and expenditure category), and any changes between budget categories must be approved by the DFA and the LFC.

Investments— Investments are recorded at fair value. The estimated fair value of investments is based on quoted market prices, except for certain alternative investments for which quoted market prices are not available. The estimated fair value of these alternative investments is based on the most recent valuations provided by the external investment managers, adjusted for cash receipts, cash disbursements, and securities distributions through June 30, 2009. The Board believes the carrying amount of these financial instruments is a reasonable estimate of the fair value. Because alternative investments are not readily marketable, their estimated value is subject to uncertainty and therefore may differ from the value that would have been used had a ready market for such investments existed.

There are certain market risks, credit risks, foreign exchange currency risks, or events that may subject the Plan's investment portfolio to economic changes occurring in certain industries, sectors, or geographies.

Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date.

The Board's investments in limited partnerships are valued at estimated fair value based on their proportionate share of the partnerships' fair value as recorded in the partnerships' audited financial statements. The limited partnerships allocate gains, losses and expenses to the partners based on the ownership percentage as described in the partnership agreements. At June 30, 2009, the Board had commitments for additional future contributions to the limited partnerships totaling $521.4 million.

Net investment income includes net appreciation (depreciation) in the fair value of investments, interest income, dividend income, securities lending income, and investment expense, which includes management and custodial fees, securities lending expense, and all other significant investment-related costs.

Other investments, as presented in the Statements of Plan Net Assets, include investments in swap agreements, distressed debt, option agreements, real estate investment trusts, and timber partnerships.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Capital Assets—Capital assets represent the cost of assets, net of accumulated depreciation, used for the administration of the Plan. Capital assets include the Board's administration building located in Santa Fe, New Mexico. The Board's capitalization policy, based on the requirements from Section 12-6-10 NMSA 1978, is to include all assets with a useful life of more than one year and costing $5,000 and greater. Assets less than $5,000 but categorized as sensitive, primarily IT equipment, are also capitalized for tracking and control purposes. All additions are capitalized at historical cost as of the date of acquisition, and depreciation is calculated on a straight-line basis over the asset's estimated useful life with no salvage value.

Estimated useful lives are as follows:

Building and building improvements	25 years
Depreciable land improvements	10 years
Furniture and equipment	10 years
Data processing equipment (including software)	5 years

Funds Held for Others—Payments from members pursuant to agreements to purchase service credits are recorded as funds held for others until the purchase agreements have been completed. Upon receipt of all payments necessary to complete the purchase agreement service credit is recorded in the member's individual account and revenue is recognized in the appropriate revenue accounts for contributions, return of interest previously withdrawn, or interest charged on restoration of service.

Refunds Payable—Refunds payable represents amounts due to terminated members who have submitted a valid claim for refund, but who have not been paid on or before the end of the fiscal year.

Funding Policy - Funding of the retirement plan is accomplished through member and employer contributions and the investment earnings on these contributions. The contribution rate is set by statute for both members and for the employers. The funding period is determined, as described below, using the Entry Age Normal actuarial cost method.

The Entry Age Normal actuarial cost method assigns the plan's total unfunded liabilities (the actuarial present value of future benefits less the actuarial value of assets) to various periods. The unfunded actuarial accrued liability is assigned to years prior to the valuation, and the normal cost is assigned to the year following the valuation. The remaining costs are the normal costs for future years. Each year's contribution is composed of (i) that year's normal cost, plus (ii) a payment used to reduce the unfunded actuarial accrued liability.

The normal cost is the level (as a percentage of pay) contribution required to fund the benefits for a new member. This is determined based upon a hypothetical group of new entrants. This group is based on the age-pay-sex distribution at hire for members joining ERB during the five-year period ending June 30, 2004. Part of the normal cost is paid from the employees' own contributions. The employers pay the balance from their contributions. In the calculation of the normal cost, the benefit provisions applicable to future new members were used.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The actuarial accrued liability is the difference between the total present value of future benefits and the actuarial present value of future normal costs. The unfunded actuarial accrued liability is the excess of the actuarial accrued liability over the actuarial value of the assets.

The balance of the employers' contribution - the remainder after paying their share of the normal cost - is used to reduce the unfunded actuarial accrued liability. The funding period is the length of time required for the unfunded actuarial accrued liability to be completely amortized, assuming that the portion used to reduce the unfunded remains level as a percentage of total payroll, which is assumed to grow 3.75% per year. The 3.00% contribution made by employers to ERB on behalf of employees who elected to participate in the Alternative Retirement Plan is also used to amortize the unfunded actuarial accrued liability.

It is assumed that all contribution are made monthly at the end of the month.

Active member payroll was projected to increase 3.75% a year for the purpose of determining the funding period. This estimate is consistent with the base rate of increase in salaries used to calculate actuarial present values.

The valuation assets used for funding purposes is derived as follows: The actuarial value of assets is based on the market value of assets with a five-year phase-in of actual investment return in excess of (less than) expected investment income. Expected investment income is determined using the assumed investment return rate and the market value of assets (adjusted for receipts and disbursements during the year). Returns are measured net of all investment and administrative expenses.

As required under GASB Statement Number 50, *Pension Disclosures (an amendment of GASB 25 and 27)*, the following is a Schedule of Funding Progress using the entry age normal funding method to illustrate the funding status of the retirement plan.

The funded status of the ERB plan at June 30, 2009 is as follows (dollar amounts in millions):

Actuarial Assets	Actuarial Accrued Liability	Unfunded Actuarial Accrued Liability	Funded Ratio	Covered Payroll	Unfunded Actuarial Accrued Liability as a Percentage of Covered Payroll
(a)	(b)	(b) - (a)	(a)/(b)	(c)	((b-a)/c)
$9,366.3	$13,883.3	$4,517.0	67.5%	$2,585.7	174.7%

The required Schedule of Funding Progress immediately following the notes to the financial statements presents 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.

NOTE 3. INTEREST IN STATE GENERAL FUND INVESTMENT POOL AND CASH DEPOSITS

Investment in State General Fund Investment Pool

The Board is required by statute to remit any money received for or on behalf of the Plan into its own account at the New Mexico State Treasury. Excess money at the end of the day in the Board's account at the New Mexico State Treasury is pooled and invested by the Office of the New Mexico State Treasurer in overnight repurchase agreements. Accordingly the investments of the Department consist of an interest in the investment pools managed by the New Mexico State Treasurer's Office.

All repurchase agreements are collateralized by the U.S. Treasury securities held by the New Mexico State Treasurer's custodian bank. The amount deposited as of June 30, 2009 and 2008 with the New Mexico State Treasurer's Office was $17,627,763 and $4,990,356, respectively.

Interest Rate Risk - The State Investment Pool does not have an investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk - The New Mexico State Treasurer pools are not rated. For additional GASB 40 disclosure information regarding cash held by the State Treasurer, the reader should see the separate audit report for the State Treasurer's Office for the fiscal year ended June 30, 2009.

Cash Deposits

In addition to the overnight investment at the New Mexico State Treasury, the Board invests in the Short-Term Investment Fund ("STIF"), held by Northern Trust. The STIF is used to facilitate more efficient trade procedures with the Board's external money managers. Net cash balances in each internal and external investment manager's portfolio are swept into the STIF at the end of each day. STIF investments and cash of $289,479,681 and $346,040,280 as of June 30, 2009 and 2008, respectively, are considered cash equivalents and are reported as cash and short term investments balances in the statements of plan net assets.

Custodial Credit Risk - Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the Board will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The Board does not have a deposit policy for custodial credit risk. As of June 30, 2009 and 2008, there were no cash balances exposed to custodial credit risk. All cash is invested in a mutual fund consisting of 100% U.S. Treasury securities.

NOTE 4. INVESTMENTS

The Board is authorized to invest or reinvest the fund in accordance with the Uniform Prudent Investor Act (45-7-601 NMSA 1978).

The Uniform Prudent Investor Act does the following:

A. Sets a higher standard of care and prudence for investments, above and beyond the previous standard and guiding principles of law

B. Applies to the trust as a whole, rather than individual investments

C. Requires investment strategy to be based on suitable risk and reward strategies

D. Requires diversification unless the trustees reasonably determine it is not in the best interest of the fund/trustees

Investments of the Board as of June 30, is as follows:

Investment Description	**2009**	**2008**
Investments held by the Board's agent in the name of the Board:		
U.S. Government and Agency Securities	$ 582,853,782	$ 502,464,238
Asset and Mortgage Backed Securities	350,555,573	280,538,993
Domestic Corporate Bonds	1,035,469,814	1,250,967,283
Domestic Stocks	1,702,981,085	2,885,840,099
International Stocks	1,236,942,856	1,580,072,169
Hedge Funds	537,791,270	722,726,369
Private Equity	138,357,638	93,682,458
Private Real Estate	77,902,570	34,450,129
Other Investments	545,166,380	2,564,355
Total	$ 6,208,020,968	$ 7,353,306,093
Investments Held by Broker/Dealers Under Securities Loaned with Cash Collateral:		
U.S. Governments and Agency Securities	$ 261,341,096	$ 428,963,257
Domestic Corporate Bonds	8,900,616	6,482,619
Domestic Stocks	377,811,235	660,963,459
International Equities	1,873,561	3,609,596
Securities Lending Collateral Investments	665,254,810	1,122,436,801
Total	1,315,181,318	2,222,455,732
Total Investments	$ 7,523,202,286	$ 9,575,761,825

NOTE 4. INVESTMENTS (CONTINUED)

Foreign Currency Risk—Foreign currency risk for investments is the risk that changes in exchange rates will adversely affect the investments. Foreign currency risk is present in the Board's investment in foreign equity securities. Managers of these assets are given discretion to hedge this risk. The maximum exposure to foreign currency risk as of June 30, 2009 was $961,780,876. The Board's investment exposure to foreign currency risk as June 30, 2008 was $1,463,147,777.

Exposure to foreign currency risk as of June 30, 2009 is as follows:

Currency	Equity Securities	Cash (overdraft)
Australian Dollar	$ 21,084,409	$ 14,044
Brazilian Real	73,186,580	(741,683)
British Pound Sterling	107,685,900	3,851,363
Canadian Dollar	5,387,970	141,321
Czech Koruna	4,368,479	28,868
Denmark Krone	4,045,715	-
Egyptian Pound	4,470,278	-
Euro	221,052,583	(21,143,183)
Hong Kong Dollar	128,699,369	5,480,351
Hungarian Forint	2,525,284	29,975
Indonesian Rupiah	8,147,300	117,280
Japanese Yen	89,208,170	10,793
Malaysian Ringgit	6,824,706	-
Mexican Peso	8,033,724	105,401
New Israeli Sheket	16,694,192	100,854
Norwegian Krone	8,288,339	89,184
Philippine Peso	717,997	29,668
Polish Zloty	1,030,639	425
Singapore Dollar	5,621,811	35,929
South African Rand	58,268,382	442,357
South Korean Won	107,219,675	(75,302)
Swedish Krona	4,744,644	10,805
Swiss Franc	27,716,692	41,515
Thai Baht	12,185,324	(62,273)
Turkish Lira USD	29,954,917	(249,051)
Total Foreign Exposure	957,163,079	(11,741,359)
Investments not subject to foreign currency risk	6,566,039,207	301,220,133
Total Investments	$ 7,523,202,286	$ 289,478,774

NOTE 4. INVESTMENTS (CONTINUED)

Exposure to foreign currency risk as of June 30, 2008 is as follows:

Currency	Equity Securities	Cash (overdraft)
Argentina	3,598,292	1,140
Australian Dollar	$ 67,369,716	$ -
Bahrain	548,118	-
Brazilian Real	57,755,377	145,574
Canadian Dollar	5,218,173	93,031
Chile	2,032,964	22,699
China Renminbi	30,932,894	-
Czech Republic	2,160,134	1,645
Denish Krone	14,133,430	-
Egypt	723,768	25,327
Euro	431,250,668	(177,299)
Hong Kong Dollar	15,213,658	277,342
Hungarian Forint	1	14,873
Indian Rupee	12,854,696	571,434
Indonesian Rupiah	4,154,401	-
Israeli Shekels	11,794,390	43,314
Japanese Yen	227,673,807	2,164,023
Korea	12,887,198	-
Malaysian Ringgit	1,512,106	45
Mexican Peso	12,680,087	47,306
Norwegian Krone	26,668,209	(455,260)
Peru Sol	2,777,227	-
Philippino Peso	1,061,864	27,618
Polish Zlotz	3,005,176	19,018
Portugal	4,799,690	-
Russia Ruble	34,278,810	-
Singapore Dollar	27,203,008	-
South African Rand	23,069,808	99,087
South Korea Won	32,595,425	357,039
Swedish Krona	10,936,111	-
Switss Franc	83,538,453	294,974
Taiwan Dollar	26,400,950	306,218
Thailand Baht	9,304,029	-
Turkish Lira	2,401,575	105,210
United Kingdom - BPS	256,363,001	266,204
	1,458,897,214	4,250,562
Investments not subject to foreign currency risk	8,116,864,611	341,784,967
Total Investments	$ 9,575,761,825	$ 346,035,529

NOTE 4. INVESTMENTS (CONTINUED)

Custodial Credit Risk—Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty, the Board will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The Board's investment policy limits holding of securities by counterparties to those involved with securities lending.

In the event of the failure of the counterparty to deliver back the borrowed securities, the Board will sell the collateral securities and offset any gains or losses with the counterparty.

All investments except securities lending collateral are held by Northern Trust (Chicago, Illinois). Investments in securities lending collateral are held by Wachovia Bank (Los Angeles, California).

Interest Rate Risk—Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Board does not have a policy for interest rate risk management. However, interest rate risk is managed through duration, by operating within defined risk parameters versus a benchmark index.

As of June 30, the Board's exposure to interest rate risk is summarized as:

Investment Type	Amount 2009	Amount 2008	Duration (In Years) 2009	2008
U.S. Treasury Sec.	$ 230,027,482	$ 166,650,949	5.67	6.74
U.S. Government & Agency Obligations	611,162,262	764,776,546	3.66	4.00
Corporate Obligations	788,727,916	1,257,449,902	4.76	5.92
Asset- & Mortgage-Backed Sec.	187,690,938	280,538,993	3.16	3.45
Guaranteed Fixed Income	8,866,119	-	2.45	
Short-Term Investments	289,479,681	346,040,280	0.45	0.45
Overall	$ 2,115,954,398	$ 2,815,456,670	4.37	4.81

The Board uses the weighted average method to determine the duration of its investments

Credit Risk—Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The general investment policies of the Board require that noncash, interest-paying securities in the high-yield bond portfolios may not exceed 5% of the market value of the portfolio and that investments in cash may represent no more than 5% of each individual fund. Credit risk is managed through diversification and by operating within defined parameters versus a benchmark index. Excluding those investments issued by or explicitly guaranteed by the U.S. government, which are not considered to have credit risk, the Board's credit quality distribution for investments with credit risk exposure at of June 30, 2009 and 2008, is summarized below. The investments were rated and categorized according to Standard & Poor's rating standards.

NOTE 4. INVESTMENTS (CONTINUED)

Summary of Investment by Rating - Credit Risk as of 06/30/09

Investment Type	Rating	Fair Market Value
Asset Backed Securities	A	$ 1,532,447
	AA	1,461,451
	AAA	12,739,412
	B	70,520
	B-	2,435,661
	B+	105,403
	B2	218,750
	B3	483,087
	BB	657,323
	BBB	2,713,896
	BBB-	1,195,171
	BBB+	1,103,773
	CCC	1,754,719
Commercial Mortgage-Backed	A	81,810
	A-	1,525,767
	A+	907,741
	A3	1,315,938
	AA	566,654
	AA-	2,985,161
	AAA	106,786,241
	BB-	301,148
	BB+	1,014,843
	BBB-	392,948
	BBB+	1,853,807
Non-Government Backed C.M.O.s	A	95,400
	A-	395,775
	A+	352,488
	AA	3,879,887
	AA-	118,355
	AAA	14,469,377
	B-	743,436
	B+	54,117
	B1	381,277
	BB	449,432
	BBB	171,404
	Caa1	1,288,910
	Caa2	521,701
	CCC	17,565,708
Total Asset and Mortgage Backed Securities		184,690,938
Bank Loans	B	13,964,391
	B-	23,031,044
	B+	28,586,372
	BB	8,821,880
	BB-	23,140,331
	CC	5,270,168
	CCC	1,244,532
	CCC+	26,276,555
	D	21,971,458
	Not Rated	13,557,904
Total Bank Loans		165,864,635

NOTE 4. INVESTMENTS (CONTINUED)

Corporate Bonds	A	$ 125,070,298
	A-	66,108,140
	A+	35,254,266
	AA	3;652,752
	AA-	16,485,177
	AA+	15,941,605
	AAA	3,784,391
	B	37,882,614
	B-	25,808,384
	B+	35,549,425
	B1	2,095,200
	Ba3	1,580,033
	Baa1	1,161,000
	Baa2	638,995
	BB	18,437,098
	BB-	35,888,395
	BB+	28,290,263
	BBB	106,228,185
	BBB-	61,814,215
	BBB+	86,531,730
	C	4,853,393
	CC	3,616,895
	CCC	15,411,339
	CCC-	4,032,520
	CCC+	18,464,994
	D	14,420,911
	Not Rated	13,350,934
Corporate Convertible Bonds	B-	5,023,788
	CCC	518,788
	CCC-	668,188
	Not Rated	164,000
Guaranteed Fixed Income	AAA	8,866,120
Common Stock	B+	2,317,290
Preferred Stock	C	535,411
Other Fixed Income	Not Rated	243,923,693
Total Domestic Corporate Securities		1,044,370,430
Government Agencies	A	3,024,252
	AAA	147,498,046
	BBB+	3,677,402
Government Mortgage Backed Securities	AAA	456,962,561
Municipal/Provincial Bonds	A	2,543,884
	AA	461,251
Total Government Agencies		614,167,396
U.S. Treasury Bonds	AAA	155,046,599
	BBB+	3,807,000
Index Linked Government Bonds	AAA	71,173,883
Total U.S. Treasury Securities		230,027,482
Other Investments Not Subject to Credit Risk		5,284,081,404
TOTAL		$ 7,523,202,286

NOTE 4. INVESTMENTS (CONTINUED)

Summary of Investment by Rating - Credit Risk as of 06/30/08

Investment Type	Rating	Fair Market Value
Asset Backed Securities	A	$ 5,784,270
	AA	4,800,050
	AAA	43,707,030
	B	2,155,031
	BA	1,562,628
	BAA	1,445,684
	CAA	155,662
Commercial Mortgage-Backed	A	3,655,713
	AA	1,638,153
	AAA	148,236,089
	BAA	544,383
Non-Government Backed C.M.O.s	A	1,465,373
	AA	6,569,844
	AAA	54,866,967
	BAA	3,952,116
Total Asset and Mortgage Backed Securities		280,538,993
Corporate Bonds	A	144,532,066
	AA	116,309,441
	AAA	311,009,183
	B	260,563,455
	BA	89,723,987
	BAA	216,474,203
	BB	23,750,039
	BBB	6,242,770
	C	713,797
	CA	4,501,021
	CAA	59,109,930
	CC	2,533,239
	CCC	1,286,250
	Not Rated	20,837,683
Corporate Convertible Bonds	CAA	86,400
Fixed Income Derivatives - Options	Not Rated	(223,562)
Total Domestic Corporate Bonds		1,257,449,902
Government Agencies	AA	2,992,201
	AAA	66,282,629
Government Mortgage Backed Securities	AAA	618,227,050
Index Linked Government Bonds	AAA	70,058,253
Municipal/Provincial Bonds	AA	639,570
	AAA	1,188,668
Other investments classified as Government Agency Securities but not subject to credit risk		5,388,175
Total Government Agencies		764,776,546
Government Bonds	AAA	162,940,887
	BAA	3,710,062
Total U.S. Treasury Securities		166,650,949
Other Investments Not Subject To Credit Risk		7,106,345,435
TOTAL		$ 9,575,761,825

NOTE 4. INVESTMENTS (CONTINUED)

Cash Balances —The Board earns interest on all monies held at the custodial agent bank. When a security purchase transaction fails to be completed due to the broker not delivering the purchased security on settlement date the cash remains with custodial agent bank. When this occurs, the Board's money is invested overnight in a Short-Term Investment Fund (STIF).

Concentration Risk—Concentration risk is identified by the amount of investment in any one issuer that represents 2% or more of plan net assets. As of June 30 2009 and 2008, with the exception of U. S. Government and Agency securities, the Board was not exposed to any concentration risk greater than 2%.

NOTE 5. DERIVATIVE INSTRUMENTS

Derivatives are generally defined as contracts or securities whose value depend on, or derives from, the value of an underlying asset, reference rate, or index. The Plan invests in the following types of Derivative Instruments.

Asset Backed Securities—In accordance with investment policy and fiduciary principles, the Plan invests in various forms of asset backed securities that fit the previous definition of derivative securities as follows:

	2009	2008
Asset Backed Securities	$ 26,471,613	$ 59,739,465
CMO's	$ 65,952,539	$102,501,735
Commercial Mortgage Backed securities	$117,732,059	$154,867,845

Foreign Currency Exchange Contracts—The Board may enter into forward contracts to purchase and sell foreign currencies in the normal course of its investing activities to manage the currency exposure associated with the Board's foreign equity and fixed income investments. The terms of these contracts generally do not exceed one year. The credit risk associated with these contracts is minimal as they are entered into with a limited number of highly rated counterparties.

Futures Contracts—The Board enters into futures contracts in the normal course of its investing activities to manage market risk associated with the Plan's equity and fixed income investments and to achieve overall investment portfolio objectives. These contracts involve elements of market risk in excess of amounts recognized in the Statements of Plan Net Assets. The credit risk associated with these contracts is minimal as they are traded on organized exchanges and settled daily.

NOTE 5. DERIVATIVE INSTRUMENTS (CONTINUED)

During 2009, the Board was a party to futures contracts held for trading purposes for U.S. Treasury bonds and 90 day Euro dollar fixed income futures. Upon entering into a futures contract, the Board is required to deposit either in cash or securities an amount ("initial margin") equal to a certain percentage of the nominal value of the contract. Subsequent payments are then made or received by the Board, depending on the daily fluctuation in the value of the underlying contracts. FNMA Discount Notes owned and included in the investments of the Board, with a value of approximately $1,399,387 and $1,940,744 at June 30, 2009 and 2008, respectively, were held by the Plan's brokers as performance security on futures contracts.

FY 09
Summary of Outstanding Futures Contracts

	No. of Contracts	Notional Amount
Futures Contracts - Long	1115	$ 762,413,750
Futures Contracts - Short	-	$ -

	Fair Value
Margin Deposit	$ 1,339,387

FY 08
Summary of Outstanding Futures Contracts

	No. of Contracts	Notional Amount
Futures Contracts - Long	944	$ 123,256,836
Futures Contracts - Short	885	$ 885,000,000

	Fair Value
Margin Deposit	$ 1,940,744

Options – An option contract is a contract in which the writer of the option grants the buyer of the option the right to purchase from ("call option"), or sell to ("put option"), the writer a designated instrument at a specified price within a specified period of time. Both written and purchased options were used by the Board during 2009. When the Board purchases or writes an option, an amount equal to the premium paid or received by the plan is recorded as an asset or liability and is subsequently adjusted to the current market value of the option purchased or written. Gain or loss is recognized when the option contract expires or is closed. As of June 30, 2009, the value of open written and purchased options was approximately $136,600 and $132,825, respectively. As of June 30, 2008, the value of open written and purchased options was approximately $452,100, and $457,300, respectively.

Swap Contracts — Swap contracts are executed on a number of different bases. The two types employed by the Board on June 30, 2009, were interest rate swap contracts and credit default swap contract. An interest rate swap contract is an agreement between two parties to exchange periodic interest payments. One party agrees to make payments to the other based on a fixed rate of interest in exchange for payments based on a variable rate. ERB employs interest rate swap contracts to adjust fixed income portfolio durations.

NOTE 5. DERIVATIVE INSTRUMENTS (CONTINUED)

Swap Contracts (continued) — A credit default swap contract is similar to an insurance policy, with the credit risk of an individual issuer or a basket of issuers (the "reference asset") the insured factor. Under such a contract, two parties enter into an agreement whereby the first party pays the second party a fixed periodic payment for the specified life of the contract (analogous to an insurance premium). The other party makes no payment unless a credit event related to the reference asset occurs. If such an event takes place, the second party is obligated to make a payment to the first party. The size of the payment is linked to the decline in the reference asset's market value following determination of the occurrence of a credit event.

Hedge Funds — In addition, the use of other derivatives is allowed under the Hedge Fund Investment Policy.

NOTE 6. SECURITIES LENDING

The Board or its designated agent may enter into contracts for the temporary exchange of securities for the use by brokers/dealers, banks, and other recognized institutional investors for periods not to exceed one year, for a specified fee or consideration. Securities lent include fixed income securities and domestic equities. No such contract shall be entered into unless the contract is fully secured by a collateralized, irrevocable letter of credit running to the Board; cash; or equivalent collateral of at least 102% of the market value of the securities plus accrued interest temporarily exchanged. This collateral shall be delivered to the State fiscal agent or its designee contemporaneously with the transfer of funds or delivery of the securities. Such contract may authorize the Board to invest cash collateral in instruments or securities that are authorized fund investments and may authorize payment of a fee from the Plan or from income generated by the investment of cash collateral to the borrower of securities providing cash as collateral. The Board may apportion income derived from the investment of cash collateral to pay its agent in securities lending transactions.

At year-end, the Board has no net credit risk exposure to borrowers, because the amounts the Board owes the borrowers exceed the amount the borrowers owe the Board. The contract with the Board's agent requires it to indemnify the Board fully if the borrowers fail to return the securities (and if the collateral is inadequate to replace the securities lent) or fail to pay the Board for income distributions by the securities' issuers while the securities are on loan. The Board has not experienced any losses due to credit or market risk on securities lending activities since the implementation of this program. The Board received net securities lending income totaling $4,772,872 and $5,864,540 for the fiscal years ended June 30, 2009 and 2008, respectively.

NOTE 6. SECURITIES LENDING (CONTINUED)

The collateral information as of June 30, 2009 and 2008 is summarized as follows:

Securities On Loan	Underlying Securities	Collateral Received	Collateral Investment Value
2009:			
Lent for cash collateral:			
U.S. Government & Agency Sec.	$ 261,341,096	$ 266,189,046	$ -
U.S. Equities	377,811,235	396,787,461	-
Int'l Equities	1,873,561	6,162,167	-
U.S. Corporate Obligations with Variable Rates	8,900,616	9,055,750	302,480,751
Asset-Backed Sec. with Variable Rates	-	-	209,774,059
Repurchase Agreements	-	-	153,000,000
	$ 649,926,508	$ 678,194,424	$ 665,254,810

Securities On Loan	Underlying Securities	Collateral Received	Collateral Investment Value
2008:			
Lent for cash collateral:			
U.S. Government & Agency Sec.	$ 428,963,257	$ 441,553,866	$ 3,361,287
U.S. Equities	660,963,459	684,465,920	-
Int'l Equities	3,609,596	3,654,604	-
U.S. Corporate Obligations with Variable Rates	6,482,619	6,689,320	438,875,515
Asset-Backed Sec. with Variable Rates	-	-	397,199,999
Repurchase Agreements	-	-	283,000,000
	$ 1,100,018,931	$ 1,136,363,710	$ 1,122,436,801

The Board is permitted to loan securities under (1) open loans, which are generally overnight loans, and (2) term loans with specified expected termination dates. Cash collateral is invested in traditional money market instruments. The policy is to match the maturities of investments made with the cash collateral to the maturities of the loan agreements. The Board cannot pledge or sell collateral securities received unless the borrower defaults, and therefore, the Board does not establish an asset and a corresponding liability in the balance sheet for the collateral value of securities received. There were no significant violations of legal or contractual provisions and no borrower or lending agent default losses.

NOTE 7. CAPITAL ASSETS

Capital assets relate to all assets of the Board that are used in operations and have useful lives extending beyond a single reporting period. Capital assets in progress at June 30, 2008 represent costs to date on the second phase of the addition and modifications to the Santa Fe offices. With project completion in 2009, these costs were transferred to other asset classifications. There were no capital assets in progress at June 30, 2009.

Depreciation expense was $2,050,969 and $1,503,248 for the years ended 2009 and 2008, respectively. Capital asset activity for the years ended June 30, 2009 and 2008 is as follows:

	Beginning Balance	Additions	Deletions	Ending Balance
2009:				
Land	$ 248,172	$ -	$ -	$ 248,172
Capital assets in progress	1,176,211	-	1,176,211	-
Depreciable land improvements	19,361	-	-	19,361
Building and building improvements	2,151,067	1,214,647	-	3,365,714
Furniture and equipment	1,078,738	88,733	58,952	1,108,519
Other Assets (Art in Public Places)	-	30,500	-	30,500
Integrated Retirement Information System (IRIS)	9,156,963	-	-	9,156,963
Total	13,830,512	1,333,880	1,235,163	13,929,229
Accumulated depreciation:				
Depreciable land improvements	2,412	699	-	3,111
Building and building improvements	1,011,482	115,344	-	1,126,826
Furniture and equipment	740,461	103,534	57,525	786,470
Integrated Retirement Information System (IRIS)	1,954,689	1,831,392	-	3,786,081
Total	3,709,044	2,050,969	57,525	5,702,488
Capital assets—net	$ 10,121,468	$ (717,089)	$ 1,177,638	$ 8,226,741

NOTE 7. CAPITAL ASSETS (CONTINUED)

	Beginning Balance	Additions	Deletions	Ending Balance
2008:				
Land	$ 248,172	$ -	$ -	$ 248,172
Capital assets in progress	6,396,673	1,176,211	6,396,673	1,176,211
Depreciable land improvements	1,875	17,486	-	19,361
Building and building improvements	2,151,067	-	-	2,151,067
Furniture and equipment	1,087,812	141,779	150,853	1,078,738
Integrated Retirement Information System (IRIS)	-	9,156,963	-	9,156,963
Total	9,885,599	10,492,439	6,547,526	13,830,512
Accumulated depreciation:				
Capital Assets In Progress	629,350	-	(629,350)	-
Depreciable land improvements	1,688	724	-	2,412
Building and building improvements	846,467	165,015	-	1,011,482
Furniture and equipment	879,145	12,170	150,854	740,461
Integrated Retirement Information System (IRIS)	-	1,325,339	629,350	1,954,689
Total	2,356,650	1,503,248	150,854	3,709,044
Capital assets—net	$ 7,528,949	$ 8,989,191	$ 6,396,672	$ 10,121,468

NOTE 8. DUE TO EMPLOYERS AND OTHER STATE AGENCIES

This account represents the amount due to various participating public employers for over remittances of employer contributions during the fiscal years ended June 30, 2009 and 2008. Over remittances can be applied to future reporting periods or refunded, at the option of the administrative unit, in the next fiscal year. There were no amounts due to other state agencies as of June 30, 2009 or 2008.

NOTE 9. ACCRUED COMPENSATED ABSENCES

Qualified employees are entitled to accumulate vacation leave according to a graduated leave schedule of 80 to 160 hours per year, depending upon the length of service and the employee's hire date. A maximum of 30 working days (equivalent to 240 hours) of such accumulated vacation leave can be carried forward into the beginning of the next calendar year. Any excess accumulated vacation leave is forfeited.

When employees terminate employment with the State, they are compensated for accumulated vacation leave as of the termination date, up to a maximum of 240 hours. All balances up to 240 hours for each employee have been recorded at their current pay rate as of June 30, 2009 and 2008.

NOTE 9. ACCRUED COMPENSATED ABSENCES (CONTINUED)

Qualified employees are entitled to accumulate sick leave at the rate of one day for each calendar month of service. There is no limit to the amount of sick leave an employee can accumulate. Once per fiscal year, in either January or July, employees may elect to be paid for accrued sick leave in excess of 600 hours but less than 720 hours at 50% of their current hourly rate.

In the case of retiring employees, they may be paid for accrued sick leave in excess of 600 hours but less than 1,000 hours at 50% of their current hourly rate. All sick leave balances in excess of 600 hours but less than 720 hours for each employee have been recorded as a liability at 50% of their current hourly rate.

The following table provides a summary for the fiscal years ended June 30, of the change in accrued compensated absences:

	2009	2008
Balance payable—beginning of fiscal year	$ 211,914	$ 191,487
Additions	398,226	393,557
Deletions	(411,279)	(373,130)
Balance payable—end of fiscal year	$ 198,861	$ 211,914
Amount due within one year, estimated at 97%	$ 192,895	$ 205,557

Funds used to liquidate this liability will come from the ERB Retirement Plan.

NOTE 10. LEASES

The Board leases mailing and copier equipment, office space, and storage space under operating leases. Operating leases do not give rise to property rights or leases obligations; therefore, the amounts of the Board's lease agreements are not reflected on the Statements of Plan Net Assets. Leases are subject to future appropriations and are cancelable by the Board at the end of each fiscal year with 30 days' written notice to the lessor. The following table summarizes the Board's future minimum lease payments:

Years Ending June 30,	
2010	$ 80,730
2011	80,730
2012	65,415
2013	8,256
2014	1,036
Total	$236,167

Lease expense was $78,302 and $77,214 for the fiscal years ended June 30, 2009 and 2008, respectively.

NOTE 11. RETIREMENT PLANS

Employees of the Board who do not possess a teaching or administrative certificate have the option of participating in the Educational Employees Retirement Plan or the Public Employees Retirement Plan. Some employees of the Board have elected to participate in the Educational Employees' Retirement Plan ("the ERB plan") through the Educational Retirement Act , while others have elected to participate in the Public Employees Retirement Plan ("the PERA Plan") through the Public Employees Retirement Act ("PERA") of the State.

Public Employees Retirement Association (PERA). Certain full-time employees elect to participate in a public employee retirement system authorized under the Public Employees Retirement Act (Chapter 10, Article 11, NMSA 1978). The Public Employees Retirement Association (PERA) is the administrator of the plan, which is a cost-sharing multiple-employer defined benefit retirement plan. The plan provides for retirement benefits, disability benefits, survivor benefits and cost-of-living adjustments to plan members and beneficiaries. PERA issues a separate, publicly available financial report that includes financial statements and required supplementary information for the plan. That report may be obtained by writing to PERA, P.O. Box 2123, Santa Fe, NM 87504-2123. The report is also available on PERA's website at www.pera.state.nm.us.

Funding Policy. Plan members are required to contribute 7.42% of their gross salary. The Board is required to contribute 16.59% of the gross covered salary. The contribution requirements of plan members and the Board are established in State statute under Chapter 10, Article 11, NMSA 1978. The requirements may be amended by acts of the legislature. The plan members and Board's contributions to PERA for the fiscal years ending June 30, 2009, 2008 and 2007 were $590,423, $585,163, and $515,435, respectively, which equal the amount of the required contributions for each fiscal year.

Educational Retirement Board. Certain full-time employees elect to participate in a public employee retirement system authorized under the Educational Retirement Act (Chapter 22, Article 11, NMSA 1978). The Educational Retirement Board (ERB) is the administrator of the plan, which is a cost-sharing multiple-employer defined benefit retirement plan. The plan provides for retirement benefits, disability benefits, survivor benefits and cost-of-living adjustments to plan members (certified teachers, and other employees of State public school districts, colleges and universities) and beneficiaries. ERB issues a separate, publicly available financial report that includes financial statements and required supplementary information for the plan. That report may be obtained by writing to ERB, P.O. Box 26129, Santa Fe, NM 87502. The report is also available on ERB's website at www.nmerb.org.

NOTE 11. RETIREMENT PLANS (CONTINUED)

Funding Policy. Plan members are required to contribute 7.9% of their gross salary. The Board is required to contribute 11.65% of the gross covered salary. Effective July 1, 2009, plan members earning over $20,000 annually are required to contribute 9.4% of their gross salary and employees earning $20,000 or less are required to contribute 7.9%. The employer contribution will increase .75% each year until July 1, 2011 when the employer contribution will be 13.9%. The contribution requirements of plan members and the Board are established in State statute under Chapter 22, Article 11, NMSA 1978. The requirements may be amended by acts of the legislature. The plan member's and Board's contributions to ERB for the fiscal years ending June 30, 2009, 2008, and 2007, were $13,915, $2,590, and $13,134, respectively, which equal the amount of the required contributions for each fiscal year.

NOTE 12. POST-EMPLOYMENT BENEFITS – STATE RETIREE HEALTH CARE PLAN

Plan Description: The Board contributes to the New Mexico Retiree Health Care Fund, a cost-sharing multiple-employer defined benefit post employment healthcare plan administered by the New Mexico Retiree Health Care Authority (RHCA). The RHCA provides health care insurance and prescription drug benefits to retired employees of participating New Mexico government agencies, their spouses, dependents, and surviving spouses and dependents. The RHCA Board was established by the Retiree Health Care Act (Chapter 10, Article 7C, NMSA 1978). The Board is responsible for establishing and amending benefit provisions of the healthcare plan and is also authorized to designate optional and/or voluntary benefits like dental, vision, supplemental life insurance, and long-term care policies.

Eligible retirees are: (1) retirees who make contributions to the fund for at least five years prior to retirement and whose eligible employer during that period of time made contributions as a participant in the RHCA plan on the person's behalf, unless that person retires before the employer's RHCA effective date, in which the event the time period required for employee and employer contributions shall become the period of time between the employee's effective date, and the date of retirement; (2) retirees defined by the Act who retired prior to July 1, 1990; (3) former governing authority members who served at least four years.

The RHCA issues a publicly available stand-alone financial report that includes financial statements and required supplementary information for the post employment healthcare plan. That report and further information can be obtained by writing to the Retiree Health Care Authority at 4308 Carlisle NE, Suite 104, Albuquerque, NM 87107.

NOTE 12. POST-EMPLOYMENT BENEFITS – STATE RETIREE HEALTH CARE PLAN (CONTINUED)

Funding Policy. The Retiree Health Care Act (Section 10-7C-13, NMSA 1978) authorizes the RHCA Board to establish the monthly premium contributions that retirees are required to pay for healthcare benefits. Each participating retiree pays a monthly premium according to a service based subsidy rate schedule for the medical plus basic life plan plus an additional participation fee of five dollars if the eligible participant retired prior to the employer's RHCA effective date or is a former legislator or a former governing authority member. Former legislators and governing authority members are required to pay 100% of the insurance premium to cover their claims and the administrative expenses of the plan. The monthly premium rate schedule can be obtained from the RHCA or viewed on their website at www.nmrhca.state.nm.us.

The Retiree Health Care Act (Section 10-7C-15, NMSA 1978) is the statutory authority that establishes the required contributions of participating employers and their employees. The statute requires each participating employer to contribute 1.3% of each participating employee's annual salary; each participating employee is required to contribute .65% of their salary. Employers joining the program after 1/1/1998 are also required to make a surplus-amount contribution to the RHCA based on one of two formulas at agreed-upon intervals.

The RHCA plan is financed on pay-as-you-go basis. The employer, employee and retiree contributions are required to be remitted to the RHCA on a monthly basis. The statutory requirements for the contributions can be changed by the New Mexico State Legislature.

The Board's contributions to the RHCA for the years ending June 30, 2009, 2008 and 2007 were $31,468, $30,180, and $27,267 for employer contributions and $15,734, $15,090, $13,634 in employee contributions, respectively, which equal the required contributions for each year.

NOTE 13. RISK MANAGEMENT

With the exception of investment losses, the Board is exposed to various business risks of loss for which it carries insurance through the Risk Management Division of the New Mexico General Services Department. In the event of a claim being filed, the Board is responsible for only a small deductible payment in amounts that vary according to the type of claim

NOTE 14. STATUTORY DISCLOSURES

Section 2.2.2.10P(2) of the Audit Rule 2009, 2.2.2 NMAC entitled, "Requirements for Contracting and Conducting Audits of Agencies" requires that state agencies disclose all special, deficiency, and specific appropriations. The Board received the following specific appropriations:

NOTE 14. STATUTORY DISCLOSURES (CONTINUED)

Building Remodel/Addition

Laws of 2000, 2nd S.S., Chapter 23, Section 29	$	750,000
Expended in FY 2001		(8,389)
Encumbered in FY 2001		(63,999)
Rebudgeted in FY 2002		677,612
Outstanding encumbrance from 2001		63,999
Expended in FY 2002		(8,624)
Encumbered in FY 2002		(46,986)
Rebudgeted in FY 2003		686,001
Outstanding encumbrance from 2002		46,986
Expended in FY 2003		(9,490)
Encumbered in FY 2003		(74,744)
Rebudgeted in FY 2004		648,753
Outstanding encumbrance from 2003		74,744
Expended in FY 2004		(13,871)
Encumbered in FY 2004		(60,873)
Rebudgeted in FY 2005		648,753
Outstanding encumbrance from 2004		60,873
Laws of 2002, Chapter 110, Section 58		500,000
Expended in FY 2005		(913,525)
Encumbered in FY 2005		(50,769)
Rebudgeted in FY 2006		245,332
Outstanding encumbrance from 2005		50,769
Expended in FY 2006		(71,885)
Encumbered in FY 2006, but then unencumbered and restored to ERB		(1,055)
Rebudgeted in FY 2007		223,161
Laws of 2006, Chapter 111, Section 71		500,000
Laws of 2007, Chapter 42, Section 90		1,185,188
Expended in FY 2007		(125,024)
Encumbered in FY 2007		(702,262)
Rebudgeted in FY 2008		1,081,063
Outstanding encumbrance from 2007		702,262
Expended in FY 2008		(883,174)
Encumbered in FY 2008		(3,112)
Rebudgeted in FY 2009		897,039
Outstanding encumbrance from 2008		3,112
Expended in FY 2009		(56,078)
Encumbered in FY 2009		-
Unused funding restored to ERB	$	844,073

NOTE 15. INVESTMENT PLACEMENT AGENTS

Placement agents act as intermediaries on behalf of investment managers to solicit investments in a fund. Other terms used to describe the function performed by placement agents include finder, solicitor, marketer, consultant, and broker. Large investment managers may have in-house marketing or placement agent groups, while smaller investment managers may forgo the overhead associated with maintaining such operations and retain independent firms or individuals as placement agents as needed. Some placement agents are part of a large corporation and represent that corporation's investment managers, as well as independent managers. Other placement agents are independent firms or individuals.

The role of a placement agent varies depending on the needs of the investment manager retaining the agent. As of June 30, 2009, approximately 44.2% of the ERB's total $1.305 billion private equity and fund of hedge fund investment commitments (market value of currently invested funds + remaining balance approved for investment) involved placement agents. The portion of pension fund investments in which placement agents were involved was approximately 8.1% of the ERB's total $7.114 billion investment portfolio of as of that date. Placement agent fees vary, but a typical fee is one to two percent of the amount invested in a fund. The role of placement agents became a focus of inquiry in 2009 with the indictment in New York of persons receiving fees related to pension fund investments in that state. Inquiries have expanded to public pension funds in other states, including California and New Mexico. The ERB is cooperating with investigations involving the payment of placement agent fees related to investments of the Educational Retirement Fund (the "Fund").

NMSA 1978, Section 22-11-54 requires recipients of investments by the ERB to disclose the identity of, and the fee, commission, or retainer paid to, any third-party marketer or placement agent who rendered services on behalf of the recipient in obtaining the investment. The disclosure requirements do not apply to investments in publicly traded equities or fixed-income securities. Any person who knowingly withholds the required disclosure is guilty of a fourth degree felony, punishable by a fine of not more than $20,000, imprisonment for a definite term not to exceed eighteen months, or both. The ERB informs all investment managers and placement agents soliciting investments of the disclosure requirement and the penalty for failing to disclosure. The ERB also is revising its policies regarding the use of placement agents.

The ERB does not have any direct relationships with placement agents and has not directly paid fees for such services. In addition, the ERB's investment consultants and advisors do not receive any compensation other than advisory fees paid by the ERB and do not accept compensation from investment fund managers or their placement agents. The ERB is reviewing prior investments by the Fund in which placement agent fees were paid to determine whether complete disclosure was made and whether legal action is warranted.

REQUIRED SUPPLEMENTARY INFORMATION

STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF FUNDING PROGRESS

(Unaudited)

Valuation Date June 30	(1) Actuarial Value of Assets (AVA)	(2) Actuarial Accrued Liability (AAL)	(3) Unfunded Actuarial Accrued Liability (2) - (1)	(4) Funded Ratio (1)/(2)	(5) Annual Covered Payroll	(6) Unfunded Liability Actuarial as a Percentage of Covered Payroll (3)/(5)
2004	$ 7,488.0	$ 9,927.1	$ 2,439.1	75.4%	$ 2,142.4	113.8%
2005	7,457.5	10,591.8	3,134.3	70.4%	2,209.1	141.9%
2006	7,813.9	11,436.3	3,622.4	68.3%	2,219.4	163.2%
2007	8,591.4	12,190.1	3,598.7	70.5%	2,341.1	153.7%
2008	9,272.8	12,967.0	3,694.2	71.5%	2,491.7	148.3%
2009	9,366.3	13,883.3	4,517.0	67.5%	2,585.7	174.7%

Note: Dollar amounts are in millions.

STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF EMPLOYER CONTRIBUTIONS

(Unaudited)

Fiscal Year Ended June 30	Annual Required Contribution	Percentage Contributed
2004	$ 203,937,432	92.8%
2005	243,237,303	81.3%
2006	299,967,996	75.5%
2007	364,128,448	70.3%
2008	368,196,682	79.0%
2009	375,430,722	86.2%

STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
For the Years Ended June 30, 2009 and 2008
(Unaudited)

ACTUARIAL METHODS AND SIGNIFICANT ASSUMPTIONS

The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows:

	2009	2008
Valuation date	June 30, 2009	June 30, 2008
Actuarial cost method	Entry age normal	Entry age normal
Amortization method	Level payment, open	Level payment, open
Amortization period for GASB 25 ARC**	30 years	30 years
Asset valuation method	5-year smoothed market	5-year smoothed market
Actuarial assumptions:		
Investment rate of return*	8.00%	8.00%
Projected salary increases*	5.00% to 13.50%	5.00% to 13.50%
* Includes inflation calculated at	3.00%	3.00%
Cost of living adjustments	2.00%	2.00%

**The Governmental Accounting Standards Board ("GASB") Annual Required Contribution ("ARC") for this Plan is defined as the larger of (a) the employer normal cost plus a 30-year amortization of the Unfunded Actuarial Accrued Liability ("UAAL"), and (b) the statutory employer contribution rate, plus the 3.00% contribution on behalf of ARP members. Under GASB 25, the maximum allowable amortization period is 30 years.

OTHER SUPPLEMENTAL INFORMATION

STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF REVENUES AND EXPENSES—BUDGET AND ACTUAL (NON-GAAP BASIS)
For the Year Ended June 30, 2009

	Original Budget	Final Budget	Actual Budgetary Basis	Variance— Final Budget Favorable (Unfavorable)
REVENUES:				
Other state funds	$ 32,423,300	32,953,300	32,953,300	-
TOTAL BUDGETED REVENUE	$ 32,423,300	32,953,300	32,953,300	-
EXPENSES:				
Personal services and employee benefits	$ 4,021,500	4,021,500	3,894,081	127,419
Contractual services	27,581,800	28,111,800	18,823,806	9,287,994
Other costs	820,000	820,000	790,187	29,813
TOTAL EXPENSES	$ 32,423,300	32,953,300	23,508,074	9,445,226

RECONCILIATION OF GAAP BASIS TO BUDGETARY BASIS:

Loss (revenue) GAAP basis	$ 1,000,328,799
Net depreciation in investment value	1,724,901,896
Investment advisor and custody fees	16,774,502
Current-year (loss) revenue not needed for budgeted expenses	(2,709,051,897)
Revenue (non-GAAP) budgetary basis	$ 32,953,300

Expenses GAAP basis—administrative*	$ 8,671,992
Capital outlay	157,670
Depreciation expense	(2,050,969)
Investment advisor and custody fees	16,774,502
Miscellaneous GAAP adjustments and accruals	(45,121)
Expenses (non-GAAP) budgetary basis	$ 23,508,074

*Significant revenues and non-administrative expenses are not budgeted (see note 2).

STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF CASH ACCOUNTS
As of June 30, 2009 and 2008

Educational Employees' Retirement Fund
Pension Trust Account
Funds 605 and 629

	2009	2008
Petty cash	$ 100	$ 100
Qualified Excess Benefit Arrangement Trust		
Checking Account at Wells Fargo Bank	807	4,651
Short-term investment accounts:		
Overnight repurchase agreement pool—State Treasurer	17,627,763	4,990,356
Short-Term Investment Fund—STIF	289,478,774	346,035,529
Balance per financial statements	$ 307,107,444	$ 351,030,636
Pledged collateral for Wells Fargo demand deposit account:		
Total amount on deposit at June 30	$ 807	$ 4,651
Less Federal Deposit Insurance Corporation coverage	(807)	(4,651)
Total uninsured public funds	$ -	$ -

STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF ACCOUNTABILITY IN GOVERNMENT ACT—
PERFORMANCE MEASURES
As of June 30, 2009
(Unaudited)

Type	Description	Target	Actual
Outcome	Average number of days to process refund requests	15	21
Output	Average number of days to respond to requests for benefits estimates and purchase of service requests	20	17
Outcome	Percentage of member satisfaction with seminars and trainings	95%	96%
Outcome	Average rate of return over a cumulative five-year period	8.00 %	2.40 %
Output	Percent of retirement applications processed within 60 days	95%	95%
Output	Number of benefit estimates and purchase of service requests computed annually	6,000	8,361
Output	Number of member workshops conducted	35	25
Quality	Percent of accurately computed retirements	99.5%	99.5%
Output	Percent completion of the new pension system	n/a	100%
Outcome	Funding period of UAAL in years	≤30	45

ADDITIONAL INFORMATION

Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With *Governmental Auditing Standards*

To the Members of the State of New Mexico
Educational Retirement Board
and
Mr. Hector H. Balderas
New Mexico State Auditor

We have audited the Statement of Plan Net Assets and Statement of Changes in Plan Net Assets of the State of New Mexico Educational Retirement Board (ERB) as of and for the year ended June 30, 2009, and have issued our report thereon dated December 4, 2009. We have also audited the Statement of Revenues and Expenses – Budget and Actual (Non-GAAP) for ERB presented as supplemental information for the year ended June 30, 2009, as listed in the table of contents. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered ERB's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the ERB's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the entity's internal control over financial reporting.

A *control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

To the Members of the State of New Mexico
Educational Retirement Board
and
Mr. Hector H. Balderas
New Mexico State Auditor

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether ERB's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed one instance of noncompliance or other matters that is required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of current year findings and responses as item 2009-1.

We noted a matter that is required to be reported under section 12-6-5 NMSA 1978 and is described in the accompanying schedule of findings and responses as item 2008-5.

ERB's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. We did not audit ERB's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Members of ERB's Retirement Board, the Audit Committee, management, the Department of Finance and Administration, the Legislative Finance Committee, and the State Auditor, and is not intended to be, and should not be used by anyone other than these specified parties.

Moss Adams LLP

Albuquerque, New Mexico
December 4, 2009

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF STATUS OF PRIOR YEAR AUDIT FINDINGS
Year Ended June 30, 2009

2007-4 Monitoring of Journal Entries	Resolved
2008-1 Lack of Reconciliations over General Ledger Accounts	Resolved
2008-2 Review of Internal Payroll Disbursements	Resolved
2008-3 Employee and Vendor Background Checks	Resolved
2008-4 Material Adjustments to the General Ledger after Year-End	Resolved
2008-5 Alternative Retirement Plan Documentation	Revised and Repeated

2008-5 Alternative Retirement Plan Documentation

CONDITION

The current documents governing the Alternative Retirement Plan (ARP) are inconsistent and unclear. The *ARP Operations Manual* dictates that the ARP should be operated under provisions of Section 404(a) of the Internal Revenue Code and that the ARP Document is pending IRS approval. Section 9.2 of the current plan document indicates that that the Board will be named "fiduciary" as that term is defined in "Section 401(a)(2)." Based on review of this IRS code, the reference appears to be in error as this code does not seem to apply to the document.

The Plan Document has been recently filed and approved by the IRS. In the determination letter, the IRS requested that certain provisions in the Plan Document be amended by ERB.

Additionally, ERB does not have evidence of current contracts in place with the carriers for the ARP.

CRITERIA

Best practices require that legal documents governing the ARP and ERB's responsibilities under the plan should be current, consistent, clear, and properly approved.

EFFECT

The ARP is currently operating under certain terms that are may not have been approved by the Board and which appear contradictory.

CAUSE

Management has not followed up on the plan requirements or obtained proper approval for the governing documents.

RECOMMENDATION

We recommend that management clarify the terms of the plan within the ARP Document, including the responsibilities of ERB, and obtain proper approval for the ARP Document.

2008-5 Alternative Retirement Plan Documentation (Continued)

MANAGEMENT RESPONSE

1. The ERB's Board of Trustees approved the ARP Operations Manual in 1999; that document has served as the ARP plan document. The provisions of the Operations Manual were taken from a 1991 document entitled "ARP Plan Document." No evidence has been located that the 1991 document was formally adopted by the Board of Trustees. The reference to the Board being named as a "fiduciary" appears in the 1991 ARP Plan Document, and apparently is an erroneous reference to Section 402(a)(2) of ERISA, which does not govern public retirement plans such as the ARP. That reference was not repeated in the 1999 Operations Manual and in any event, the reference is not legally material.

2. The ERB has requested and received formal approval of the ARP from the IRS for its plan. In its determination letter the IRS noted that the ERB must correct certain provisions in the ARP plan documents. The ERB is in the process of making these amendments.

3. The ARP statute was amended during the 2009 legislative session. ERB has implemented statutory amendments allowing ARP participants to switch to the regular defined benefit plan upon completing seven years of contributions to the ARP plan. In addition, ERB has informed vendors of the statutory amendments that allow ARP participants to roll over or withdraw account balances upon termination or to select alternate forms of payout upon retirement. ERB will be initiating a Request for Proposal (RFP) process to solicit new proposals from vendors to provide retirement plans under the ARP. Once vendors have been selected, ERB will finalize the ARP rule and submit any necessary plan amendments to the IRS for approval.

4. The ERB has attempted to locate contracts between the ERB and the ARP carriers. These efforts included searching ERB records and repeatedly contacting the carriers. These efforts were unsuccessful. ERB has begun the process of developing contractual documents to replace missing documents.

2009-1 Unfunded Actuarial Accrued Liability

CONDITION

At June 30, 2009, utilizing the current rates of member and employer contributions, asset experience, benefit changes, interest on the unfunded liability and retiree payments, it will take forty-five years to eliminate the unfunded amount of the actuarially accrued liability. The unfunded actuarial accrued liability increased from approximately $3.7 billion at June 30, 2008 to approximately $4.5 billion at June 30, 2009.

CRITERIA

The Governmental Accounting Standards Board (GASB) No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans* defines, for accounting purposes, the maximum acceptable period for the unfunded actuarial liability.

Per GASB No. 25, Paragraph 36, f, 1. "Maximum amortization period -- The maximum acceptable amortization period for the total unfunded actuarial liability is 30 years."

In addition, internal ERB policy requires the amortization period for the unfunded actuarial accrued liability to be less than thirty years.

EFFECT

The maximum acceptable amortization period for the unfunded actuarial accrued liability of thirty years was exceeded at June 30, 2009.

CAUSE

The primary cause of the unfunded actuarial liability in excess of thirty years is due to the net investment losses of approximately $2.1 billion over the last two fiscal years.

RECOMMENDATION

We recommend that ERB continue to monitor the unfunded actuarial liability and the related amortization period.

2009-1 Unfunded Actuarial Accrued Liability (Continued)

MANAGEMENT RESPONSE

ERB has little ability to control the UAAL or the funding period. Both the benefits and contributions are set by the legislature, and without further changes in one or the other or both, and without a major market recovery, the funding period is projected to increase significantly over the next few years, as the rest of the FY 2008 and FY 2009 losses are phased into the actuarial value of assets. However, the Board and ERB Management will continue looking at modifications to plan design and opportunities to increase contribution rates in order to decrease the Unfunded Actuarial Accrued Liability (UAAL) and the funding period. Reducing the funding period to the GASB 25 limit of 30 years is a goal that our most reasonable projections and estimates indicate will be several years in the future.

The Board has been working to address the funding status for several years. In 2005 the State Legislature passed Senate Bill 181, which gradually increased both employer and employee contribution rates over a period of time. When fully implemented in 2012, the combined contribution rate will be 21.8% of payroll. In the 2009 Legislative session, several changes to plan design were adopted that have significantly reduced the Normal Cost Percentage. These included changing retirement eligibility from either 25 years of service or age plus years of service equaling 75 (rule of 75), to 30 years of service or age plus years of service equaling 80 (rule of 80). A lower Normal Cost Percentage means less of the contributions received will be needed to fund current Normal Costs and more will work toward reducing the UAAL. A change affecting funding was also implemented, requiring employers of ERB retirees working under the Return to Work program to contribute to the fund an amount equal to both the employer share plus the employee share, although no additional retirement benefits will accrue to that member for the additional contributions. Previously employers of such employees only remitted an amount equal to the employer's share. This change will also help improve our funding. With these changes implemented, the anticipated funding period has dropped from an estimated 61.4 years at June 30, 2008, to 45.0 years at June 30, 2009.

Board staff prepared the Management's Discussion & Analysis ("MD&A"), financial statements, statements, schedules, and notes for the fiscal years ended June 30, 2009 and 2008. The contents of this report were discussed during an exit conference with the Audit Committee of the Board of Directors and management of ERB on December 4, 2009. The following individuals attended this exit conference:

Educational Retirement Board

Members of the Audit Committee –
Bruce Malott, Audit Committee Chairman
Mary Lou Cameron, Audit Committee Member

Agency Management –
Jan Goodwin, Executive Director
Jeffrey M. Riggs, Deputy Director
Bob Westervelt, Chief Financial Officer
Greg Trujillo, Information Technology Manager
Steve Vigil, ERB internal Auditor

Moss Adams LLP

Scott Eliason, Partner
Julie Alliman, Manager
Jim Cox, Senior

The contents of this report will be presented to the ERB Board of Directors as part of the regular board meeting.