



**STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD**

**FINANCIAL STATEMENTS
As of and for the Years Ended
June 30, 2014 and 2013,
And Report of Independent Auditors**

MOSS ADAMS_{LLP}

Certified Public Accountants | Business Consultants

Acumen. Agility. Answers.

**STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD**

*Financial Statements
and Other Supplementary Information
June 30, 2014 and 2013*

(With Report of Independent Auditors Thereon)

Prepared by Board Staff

AUDITED BY:

MOSS ADAMS LLP

INTRODUCTORY SECTION

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**STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD**

*Official Roster
As of June 30, 2014*

BOARD OF DIRECTORS

NAME	TITLE
Ms. Mary Lou Cameron	Chairman
Mr. H. Russell Goff	Vice-Chairman
Mr. Hipolito J. Aguilar	Secretary, Designate for Ms. Hanna Skandera, Ex-officio Member
Ms. Beulah Woodfin	Member
Mr. Bradley Day	Member
Mr. Larry Magid	Member
Mr. James B. Lewis	Ex-officio Member

ADMINISTRATIVE STAFF

Ms. Jan Goodwin	Executive Director
Mr. Rick Scroggins	Deputy Director
Mr. Chris Bulman	General Counsel
Mr. Bob Jacksha	Chief Investment Officer
Ms. Dianne L. Rossbach	Chief Financial Officer
Mr. Jon Lucero	Information Technology Manager
Ms. Kathy A. Webb	Member Services Manager

FINANCIAL SECTION

REPORT OF INDEPENDENT AUDITORS

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

Report on the Financial Statements

We have audited the accompanying Statements of Fiduciary Net Position and Statements of Changes in Fiduciary Net Position of the New Mexico Educational Retirement Board (the "ERB") as of and for the years ended June 30, 2014 and 2013, and the related notes to the financial statements, which collectively comprise the ERB's basic financial statements as listed in the table of contents. We have also audited the Schedule of Revenues and Expenses-Budget to Actual for the New Mexico Educational Retirement Board presented as supplementary information, as defined by the Government Accounting Standards Board, in the accompanying financial statements as of and for the year ended June 30, 2014, as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design 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. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the plan net position of the ERB as of June 30, 2014 and 2013, and the respective changes in financial position for the years then ended in accordance with accounting principles generally accepted in the United States of America. Also, in our opinion, the Schedule of Revenues and Expenses - Budget and Actual, presents fairly the revenues and expenses for the year ended June 30, 2014 in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, schedule of changes in the net pension liability, schedule of employers' net pension liability, schedule of employer contributions, and schedule of investment returns on pages 7 through 16 and 54 through 57, respectively, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the ERB's basic financial statements. The schedule of cash accounts, schedule of administrative, consultant, and budgeted investment expenses, and the schedule of accountability in government act – performance measures on pages 59 through 61 are presented for purposes of additional analysis and are not a required part of the basic financial statements.

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

The schedule of cash accounts, schedule of administrative, consultant, and budgeted investment expenses, and the schedule of accountability in government act – performance measures is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of cash accounts, schedule of administrative, consultant, and budgeted investment expenses, and the schedule of accountability in government act – performance measures is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated December 15, 2014 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the ERB's internal control over financial reporting and compliance.

Mess Adams LLP

Albuquerque, New Mexico
December 15, 2014

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
MANAGEMENT'S DISCUSSION AND ANALYSIS
Years Ended June 30, 2014, 2013 and 2012**

INTRODUCTION

The New Mexico Educational Retirement Board (ERB) was created by the state's Educational Retirement Act to administer the New Mexico Educational Employees' Retirement Plan (Plan). The Plan is a cost sharing, multiple employer plan established to provide retirement and disability benefits for employees of the state's public schools, institutions of higher learning, and agencies providing educational programs. The Plan is a pension trust fund of the State of New Mexico.

This section presents management's discussion and analysis of ERB's financial position and performance for the fiscal year ended June 30, 2014, including comparisons to fiscal years June 30, 2013 and June 30, 2012. It is presented as a narrative overview and analysis, and should be read in conjunction with the financial statements and other detailed information presented within the notes and supplementary information sections. Throughout the discussion and analysis units of measure (i.e. billions, millions, or thousands) are approximate, being rounded up or down to the nearest tenth of the respective unit value.

FINANCIAL HIGHLIGHTS

- **Net Position:** ERB's net fiduciary position increased \$1,154.3 million, or 11.33%, during fiscal year 2014, primarily due to appreciation in the fair market value of the markets. This improvement follows an increase of \$702.7 million, or 7.41%, during the prior fiscal year 2013. The primary element of ERB's net fiduciary position is the fair market value of the investment portfolio.
- **Return on Investments:** ERB's rate of return on investments during fiscal year 2014 was a 14.71% increase, compared with an 11.12% increase in fiscal year 2013, and a 1.87% increase in fiscal year 2012. The increases in the rate of return are due primarily to increases in market performance. The portfolio return outperformed the fund's policy index return by 0.7% during fiscal year 2014.
- **Long Term Investments:** ERB's investment holdings increased \$1,587.0 billion, or 16.81%, in fiscal year 2014 after increasing \$261.3 million, or 2.85%, in fiscal year 2013.
- **Cash and Cash Equivalents:** Total cash and cash equivalents decreased \$470.7 million as of June 30, 2014 after increasing \$429.6 million in fiscal year 2013 when compared to fiscal year 2012. It is normal for the cash balance, as of a specific date, to fluctuate as ERB adjusts investment portfolio. For example, at June 30, 2013 ERB was transitioning between fund managers, explaining the increased cash on hand for that year-end. ERB's cash target allocation range for fiscal years 2014, 2013, and 2012 was between 0% and 10%. ERB has been in compliance with its cash target allocation throughout all three years.

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
Years Ended June 30, 2014, 2013 and 2012**

- **Total Investments:** The market value of the total ERB asset portfolio at June 30, 2014 was \$11.3 billion. Fund performance is shown in the following table.

Fund Performance Summary at June 30, 2014

<u>1 Year</u>	<u>3 Year</u>	<u>5 Year</u>	<u>10 Year</u>	<u>15 Year</u>	<u>20 Year</u>	<u>25 Year</u>	<u>30 Year</u>
14.6%	9.1%	12.9%	.5%	5.6%	8.2%	8.9%	10.0%

- **Receivables:** Total receivables decreased \$28.5 million during fiscal year 2014 after increasing \$11.2 million during fiscal year 2013. The majority of changes are related to the timing of investment sales. The fiscal year 2013 increase relates to a larger volume of investments sold at or near fiscal year end as compared to fiscal year 2014 or fiscal year 2012. Securities sales and purchases in the United States equity markets are usually based on “trade date + 3 days,” meaning the transaction will settle three business days after initiation. The number of days varies in other U.S. and foreign securities markets.
- **Contributions:** Employer and member contributions increased \$82.7 million, or 15.08% in fiscal year 2014 after increasing \$4.7 million, or 0.87%, in fiscal year 2013. Annual contribution totals vary year over year based on legislative rate changes, increases (or decreases) in the number of educators reported by Local Administrative Units, and on changing economic factors. The fiscal year 2014 combined total employer and member contribution rates increased 2.95% over the combined total for fiscal 2013. The rates in place for fiscal year 2013 had remained unchanged since fiscal year 2011.
- **Benefit Payments:** ERB age and service payments to retirees, including disability benefit payments, increased \$56.6 million, or 6.98%, in fiscal year 2014 over 2013 results, and \$57.2 million, or 7.57%, in fiscal year 2013 over 2012 results. These increases mirror a consistent, though modest, increase in the retiree population and the compounding cost of living adjustments (COLA) to annuity payments as retirees reach applicable age benchmarks.
- **Net Pension Liability:** ERB’s net pension liability for fiscal year 2014 is \$5,705.1 billion. This represents a \$571.1 million, or 9.1%, decrease from the fiscal year 2013 \$6,276.8 billion balance. The 2014 net pension liability stated as a percentage of covered payroll is 209.92%. The decrease in net pension liability is primarily due to investment gains.

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
Years Ended June 30, 2014, 2013 and 2012**

➤ **GASB Updates:** The Governmental Accounting Standards Board Statements issued Statements 67 and 68 in June 2012. They address new annual accounting and financial reporting requirements for pension plans and employers.

❖ The requirements of GASB 67 include changes in presentation of the financial statements, notes to the financial statements, and required supplementary information for ERB as a cost-sharing multiple employer pension plan. Specific changes include an actuarial calculation of total and net pension liability, comprehensive footnote disclosure regarding the pension liability calculation and assumptions, and increased investment activity disclosures. ERB elected to implement these changes beginning with its June 20, 2013 financial statements. The table below represents ERB's fiduciary net pension liability and sensitivity analysis fiscal years 2014 and 2013:

	1% Decrease	Current Single Rate Assumption	1% Increase
	6.75%	7.75%	8.75%
2014	\$7,763,304,829	\$ 5,705,730,813	\$ 3,987,098,791
2013	\$ 8,286,923,513	\$ 6,276,852,149	\$ 4,599,162,126

❖ GASB 68 applies to financial reporting changes that need to be implemented at the employer level, segregating and allocating a portion of the Plan's collective net pension liability to each participating employer based on their annual contributions. GASB 68 is effective for fiscal years beginning after June 15, 2014. ERB has elected to include information regarding the employer's proportionate shares of the net pension liability, deferred outflows and inflows of resources, and pension expense as of June 30, 2014 to ensure employers will have access to the information when they are ready to begin implementation.

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
Years Ended June 30, 2014, 2013 and 2012**

CONDENSED FINANCIAL INFORMATION

Statement of Fiduciary Net Position

	FY14	FY13	FY12	FY13-FY14 \$ Difference	FY12-FY13 \$ Difference	FY13-FY14 % Difference	FY12-FY13 % Difference
Assets							
Cash and short term investments	\$ 275,904,706	\$ 746,623,052	\$ 317,056,896	\$ (470,718,346)	\$ 429,566,156	-63.05%	135.49%
Receivables	136,141,735	164,616,757	153,420,332	(28,475,022)	11,196,425	-17.30%	7.30%
Investment in state general fund investment pool	1,804,456	5,353,975	5,521,436	(3,549,519)	(167,461)	-66.30%	-3.03%
Investments—at fair value	11,026,291,924	9,439,289,300	9,177,972,688	1,587,002,624	261,316,612	16.81%	2.85%
Capital assets, net of accumulated depreciation	2,028,628	2,175,777	2,862,746	(147,149)	(686,969)	-6.76%	-24.00%
Total assets	<u>\$ 11,442,171,449</u>	<u>\$ 10,358,058,861</u>	<u>\$ 9,656,834,098</u>	<u>\$ 1,084,112,588</u>	<u>\$ 701,224,763</u>	<u>10.47%</u>	<u>7.26%</u>
Liabilities							
Current liabilities	95,858,526	166,129,255	167,669,129	(70,270,729)	(1,539,874)	-42.30%	-0.92%
Long-term liabilities (compensated absences)	237,099	230,803	203,800	6,296	27,003	2.73%	13.25%
Total liabilities	<u>96,095,625</u>	<u>166,360,058</u>	<u>167,872,929</u>	<u>(70,264,433)</u>	<u>(1,512,871)</u>	<u>-42.24%</u>	<u>-0.90%</u>
Net position restricted for pensions	<u>\$ 11,346,075,824</u>	<u>\$ 10,191,698,803</u>	<u>\$ 9,488,961,169</u>	<u>\$ 1,154,377,021</u>	<u>\$ 702,737,634</u>	<u>11.33%</u>	<u>7.41%</u>

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
Years Ended June 30, 2014, 2013 and 2012**

CONDENSED FINANCIAL INFORMATION (CONTINUED)

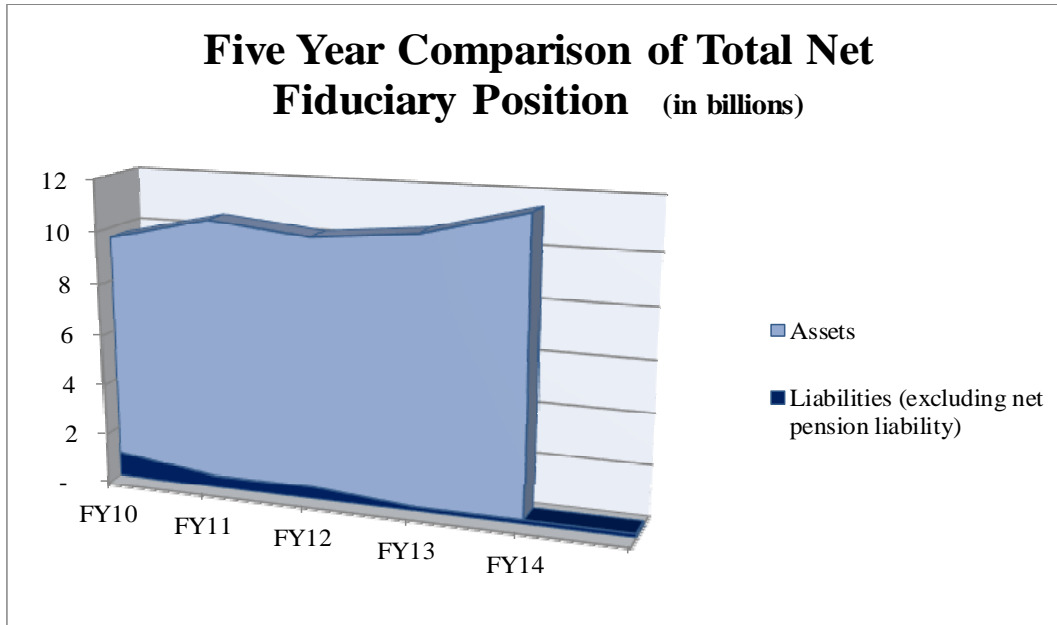
Statement of Changes in Fiduciary Net Position

	FY14	FY13	FY12	FY13-FY14 \$ Difference	FY12-FY13 \$ Difference	FY13- FY14 % Difference	FY12-FY13 % Difference
Additions							
Contributions	\$ 631,156,528	\$ 548,442,717	\$ 543,697,371	\$ 82,713,811	\$ 4,745,346	15.08%	0.87%
Investment income less investment expenses	165,707,337	179,518,742	161,326,103	(13,811,405)	18,192,639	-7.69%	11.28%
Net change in fair value of investments	1,278,664,135	837,193,133	(565,488)	441,471,002	837,758,621	52.73%	-148147.90%
Other income	2,681,458	1,898,276	3,061,710	783,182	(1,163,434)	41.26%	-38.00%
Total additions	2,078,209,458	1,567,052,868	707,519,696	511,156,590	859,533,172	32.62%	121.49%
Deductions							
Benefit payments	859,575,335	811,665,052	754,554,951	47,910,283	57,110,101	5.90%	7.57%
Refunds	47,639,130	41,664,216	40,580,979	5,974,914	1,083,237	14.34%	2.67%
Administrative expenses	16,617,970	10,985,966	11,985,538	5,632,004	(999,572)	51.27%	-8.34%
Total deductions	923,832,435	864,315,234	807,121,468	59,517,201	57,193,766	6.89%	7.09%
Net increase (decrease)	1,154,377,023	702,737,634	(99,601,772)	451,639,389	802,339,406	64.27%	-805.55%
Net position restricted for pensions							
Beginning of year	10,191,698,803	9,488,961,169	9,588,562,941	702,737,634	(99,601,772)	7.41%	-1.04%
End of year	\$ 11,346,075,824	\$ 10,191,698,803	\$ 9,488,961,169	\$ 1,154,377,021	\$ 702,737,634	11.33%	7.41%

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
Years Ended June 30, 2014, 2013 and 2012**

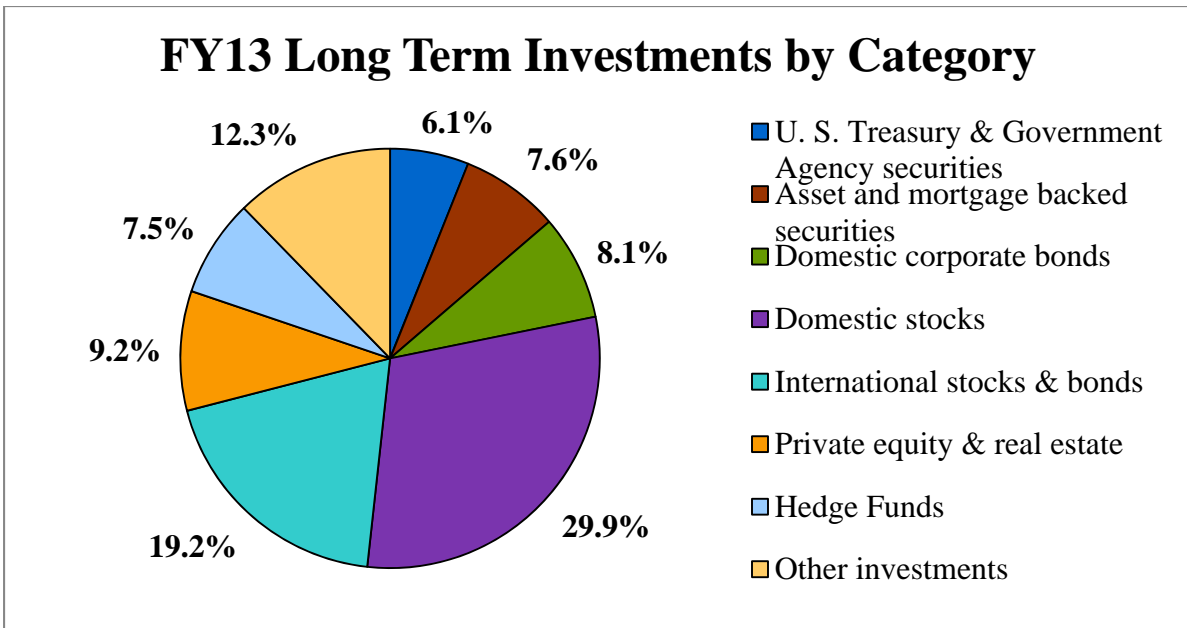
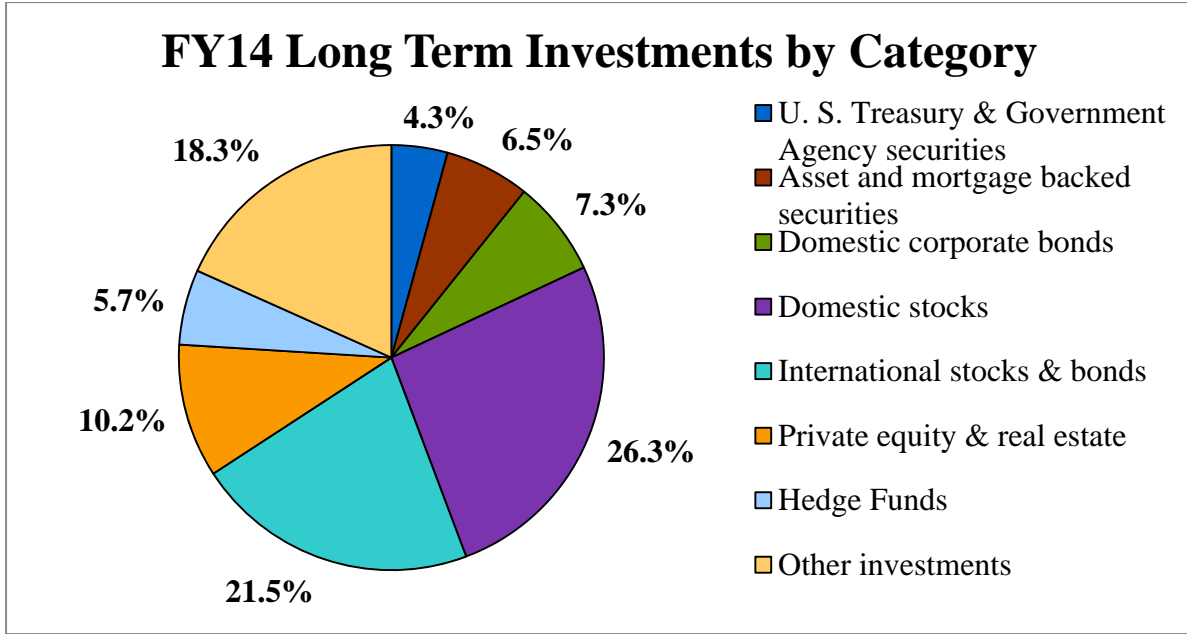
COMPARATIVE SUMMARY STATEMENTS

The following chart represents ERB's total assets relative to total liabilities, or total Net Fiduciary Position, over the last five years.

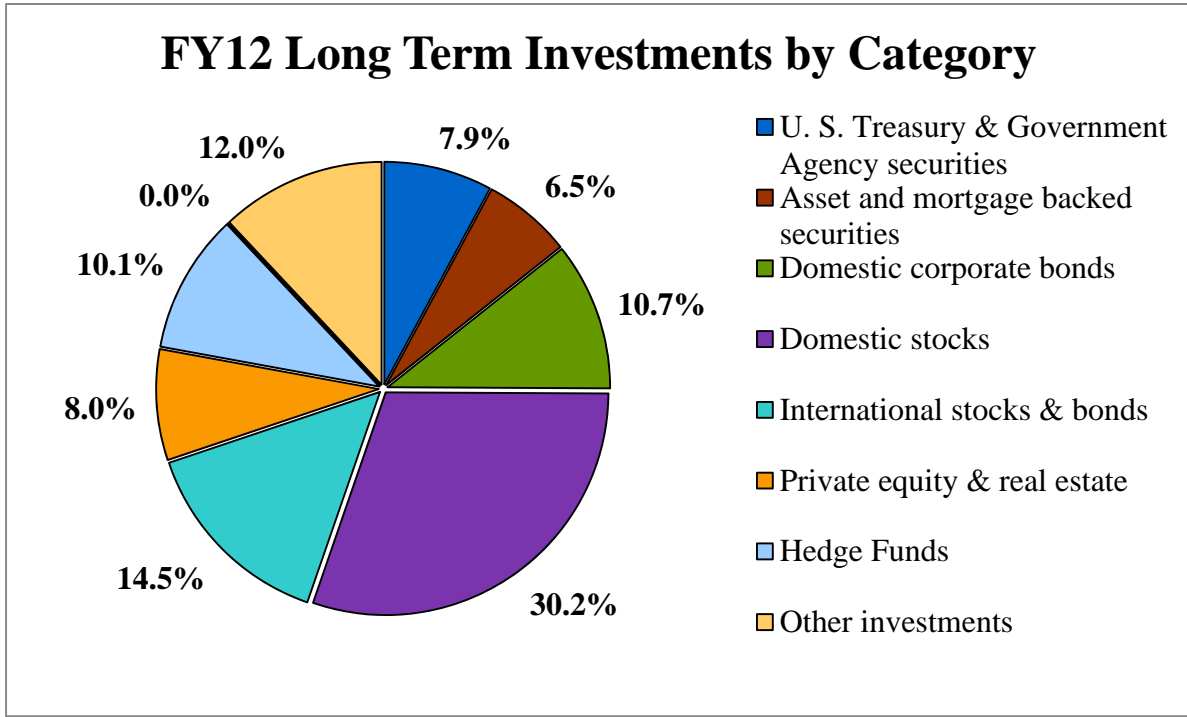


**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
Years Ended June 30, 2014, 2013 and 2012**

The following charts depict the changes in long term investment categories over the last three years. ERB adopted long term asset allocation policy benchmarks on September 20, 2012. These benchmarks were revised on June 14, 2014.



**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
Years Ended June 30, 2014, 2013 and 2012**



**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
Years Ended June 30, 2014, 2013 and 2012**

CAPITAL ASSETS

The net investment in capital assets at June 30, 2014, 2013 and 2012, is as follows:

	Cost	Accumulated Depreciation	Book Value
2014			
Land	\$ 248,172	\$ -	\$ 248,172
Depreciable land improvements	19,361	(7,043)	12,318
Integrated Retirement Information System	9,156,963	(9,156,963)	-
Building and building improvements	3,365,714	(1,746,128)	1,619,586
Furniture and equipment	1,048,595	(900,043)	148,552
Total	<u>\$ 13,838,805</u>	<u>\$ (11,810,177)</u>	<u>\$ 2,028,628</u>
2013			
Land	\$ 248,172	\$ -	\$ 248,172
Depreciable land improvements	19,361	(5,721)	13,640
Integrated Retirement Information System	9,156,963	(9,156,963)	-
Building and building improvements	3,365,714	(1,616,025)	1,749,689
Furniture and equipment	1,113,074	(948,798)	164,276
Total	<u>\$ 13,903,284</u>	<u>\$ (11,727,507)</u>	<u>\$ 2,175,777</u>
2012			
Land	\$ 248,172	\$ -	\$ 248,172
Depreciable land improvements	19,361	(5,022)	14,339
Integrated Retirement Information System	9,156,963	(8,650,910)	506,053
Building and building improvements	3,365,714	(1,514,134)	1,851,580
Furniture and equipment	1,155,929	(912,815)	243,114
Total	<u>\$ 13,946,139</u>	<u>\$ (11,082,881)</u>	<u>\$ 2,863,258</u>

LONG-TERM DEBT

The only long-term liability activity relates to compensated absences.

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
Years Ended June 30, 2014, 2013 and 2012**

CURRENTLY KNOWN FACTS AND CONDITIONS

Senate Bill 115, signed into law on March 29, 2013, included provisions applicable to the Educational Retirement Employees' pension plan. A summary of legislation that impacted the Plan is shown below:

- Raises employee contribution rates:
 - ❖ Employees with a salary over \$20,000 have a contribution rate 10.1% in FY14 and 10.7% in FY15.
 - ❖ Employees with a salary below \$20,000 have a contribution rate remaining at 7.9%.
- For new employees hired on or after July 1, 2013, they will have an actuarially reduced retirement benefit if they retire before age 55 and their COLA will be deferred until age 67.
- For new employees hired on or after July 1, 2013, the COLA begins at age 67, rather than age 65.
- For current retirees there is an immediate reduction of the COLA until the plan is 100% funded. The COLA reduction is based on the median retirement benefit (approximately \$18,500 for FY13) of all retirees excluding disability retirements. For a further description of the COLA changes please see note 2.

ERB conducts an actuarial experience study every two years. The actuarial experience study, presented to the Board of Trustees on April 26, 2013, compiled data for the six-year period ending June 30, 2013.

- Fiscal year 2014 and 2013 valuation assumptions that changed based on this study:
 - ❖ Lower wage inflation from 4.75% to 4.25%
 - ❖ Lower payroll growth from 3.75% to 3.50%
 - ❖ Minor changes to demographic assumptions
 - ❖ Population growth per year from 0.75% to 0.50%
- Assumptions that were not changed:
 - ❖ Investment return will remain at 7.75%
 - ❖ Inflation will remain at 3.00%

FINANCIAL CONTACT

Any questions regarding the financial statements of ERB should be directed to the ERB Chief Financial Officer at (505) 476-6126 or by mail at 701 Camino de los Marquez Santa Fe, New Mexico 87505.

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
STATEMENT OF CHANGES IN FIDUCIARY NET POSITION
Years Ended June 30, 2014 and 2013

	2014	2013
Assets		
Cash	\$ 211,310	\$ 23,936
Short term Investments	<u>275,693,396</u>	<u>746,599,116</u>
Receivables		
Contributions	75,926,394	65,897,831
Investment sales proceeds-brokers	45,803,653	73,812,634
Interest and dividends	13,809,329	24,271,724
Other	<u>602,359</u>	<u>634,568</u>
Total receivables	<u>136,141,735</u>	<u>164,616,757</u>
	-	
Interest in state general fund investment pool	<u>1,804,456</u>	<u>5,353,975</u>
	-	
Investments, at fair value		
Equities portfolio	4,880,406,054	3,959,409,029
Fixed income portfolio	2,376,028,406	2,399,415,954
Alternative investment portfolio	<u>3,769,857,464</u>	<u>3,080,464,316</u>
Total investments	<u>11,026,291,924</u>	<u>9,439,289,299</u>
	-	
Capital assets, at cost, net of accumulated depreciation of \$11,810,177 respectively		
	<u>2,028,628</u>	<u>2,175,777</u>
Total capital assets	<u>2,028,628</u>	<u>2,175,777</u>
Total assets	<u>\$ 11,442,171,449</u>	<u>\$ 10,358,058,860</u>
Liabilities		
Accounts payable	\$ 4,371,357	\$ 3,473,970
Accounts payable School Contributions	115,924	514,809
Accrued payroll and employee benefits	115,458	105,889
Accrued compensated absences	237,099	230,803
Refunds payable	2,613,132	1,079,930
Investment purchases payable	87,939,925	160,921,030
Funds held for others	702,728	33,627
	<u>96,095,625</u>	<u>166,360,058</u>
Total liabilities	<u>96,095,625</u>	<u>166,360,058</u>
Net assets held in trust for pension benefits	<u>\$ 11,346,075,824</u>	<u>\$ 10,191,698,802</u>

See Accompanying Notes to Financial Statements

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
STATEMENT OF CHANGES IN FIDUCIARY NET POSITION

Years Ended June 30, 2014 and 2013

	2014	2013
Additions		
Contributions		
Employer	\$ 362,462,537	\$ 299,657,530
Member	268,693,991	248,785,187
Total contributions	<u>631,156,528</u>	<u>548,442,717</u>
Investment income from investing activities		
Net change in fair value of investments	1,278,664,135	837,193,133
Interest income	41,809,254	47,709,542
Dividend income	137,617,862	147,230,301
Total investing activity gain (loss)	<u>1,458,091,251</u>	<u>1,032,132,976</u>
Investing activity expenses:		
Investment advisor fees	(13,326,824)	(14,684,190)
Custody fees	(392,955)	(736,911)
Total investing activity expenses	<u>(13,719,779)</u>	<u>(15,421,101)</u>
Net gain from investing activities	<u>1,444,371,472</u>	<u>1,016,711,875</u>
Miscellaneous Income		
Interest on restoration of service	2,819,583	1,744,359
Other	(138,125)	153,917
Total Miscellaneous Income	<u>2,681,458</u>	<u>1,898,276</u>
Total additions	<u>2,078,209,458</u>	<u>1,567,052,868</u>
Deductions		
Age and service benefit payments	859,575,335	803,253,000
Refunds to terminated members	34,561,687	35,882,999
Interest on refunds	4,361,396	5,781,217
Administrative expenses	16,617,970	10,985,967
Disability benefit payments	8,716,047	8,412,051
Total deductions	<u>923,832,435</u>	<u>864,315,234</u>
Net increase	<u>1,154,377,023</u>	<u>702,737,634</u>
Net assets held in trust for pension benefits		
Beginning of the year	<u>10,191,698,803</u>	<u>9,488,961,169</u>
End of the year	<u>\$ 11,346,075,825</u>	<u>\$ 10,191,698,803</u>

See Accompanying Notes to Financial Statements

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting—ERB’s financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting. The New Mexico General Fund 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.

Budgets and Budgetary Accounting—Formal budgetary integration is used as a management control device by ERB in administering the Plan. The budget for ERB, a New Mexico State agency is adopted on the modified accrual basis of accounting, except for prior year obligations approved for payment by the New Mexico Department of Finance and Administration per Section 6-10-4 NMSA 1978.

Each year the New Mexico Legislature approves multiple-year appropriations, which the State considers as continuing appropriations. The Legislature authorizes these appropriations for two to five years; however, it does not identify the authorized amount by fiscal year. Consequently, the appropriation is budgeted in its entirety the first year the Legislature authorizes it. The unexpended portion of the budget is carried forward as the next year’s beginning budget balance until either the project period has expired or the appropriation has been fully expended. Budget presentations in these financial statements are consistent with the State’s budgeting methodology.

Only administrative expenses and a small portion of interest income are budgeted, while significant revenues and non-administrative expenses are not. The budget 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.

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. ERB was included in performance-based budgeting for the first time in FY 2002. ERB developed performance measures which were approved by the State Budget Division (SBD), a division of New Mexico’s Department of Finance and Administration (DFA), and the Legislative Finance Committee (LFC), an interim committee of the New Mexico Legislature, and included in the General Appropriations Act. ERB is required to periodically report to the SBD and the LFC on these performance measures.

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

ERB follows these procedures in establishing the annual budget:

- (1) By August 31, staff prepares a Budget Appropriation Request to present at a Legislative Finance Committee (LFC) hearing. The Request includes proposed expenses and the means of financing them.
- (2) On September 1, the Budget Appropriation Request is submitted to the State Budget Division (SBD) of DFA and the LFC.
- (3) DFA makes recommendations and adjustments to ERB's Budget Appropriation Request, which becomes the Governor's proposal to the Legislature.
- (4) The LFC holds hearings on the Budget Appropriation Request during the Legislature's interim period. Recommendations and adjustments are made prior to presenting the Budget Appropriation Request to the Legislature.
- (5) Both DFA's and LFC's recommended appropriation proposals are presented to the Legislature for approval of the final budget. The budget approved by the Legislature is then sent to the Governor's office for final approval.
- (6) On May 1, ERB submits its annual operating budget to DFA and the LFC based on the appropriation from the Legislature and approval by the Governor.
- (7) Per Section 9 of the General Appropriation Act of 2012, all agencies, including legislative agencies, may request category transfers among personal services and employee benefits, contractual services and other. Therefore, the legal level of budgetary control would be the appropriation program level (A-Code, P-Code, R-Code, and Z-Code). The A-Code pertains to capital outlay appropriations (general obligation/severance tax or state general fund). The P-Code pertains to operating funds. The R-Code pertains to American Recovery & Reinvestment Act (ARRA) funds. The Z-Code pertains to special appropriations. ERB's budget is enacted at the P-Code level.

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, 2014.

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

ERB 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 geographic markets.

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.

ERB's investments in limited partnerships are valued at estimated fair value based on their proportionate share of the partnership's fair value as recorded in the partnership's 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, 2014, ERB had commitments for additional future contributions to the limited partnerships totaling \$2.346 billion.

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 Statement of Fiduciary Net Position, include investments in swap agreements, distressed debt, option agreements, real estate investment trusts, and timber partnerships.

The calculation of realized gains and losses is independent of the calculation of the net change in the fair value of pension plan investments. Realized gains and losses on investments that had been held in more than one reporting period and sold in the current period were included as a change in the fair value reported in the prior period(s) and the current period.

For the fiscal year ending June 30, 2014, investment fees totaled \$163,715,539; of that total \$13,719,779 was covered by the agency's operating budget and \$147,995,760 was deducted directly from investment account balances. For the fiscal year ending June 30, 2013, the investment fees totaled \$125,478,811; of that total \$17,665,292 was covered by the agency's operating budget and \$107,813,519 was deducted directly from investment account balances.

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

ERB 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. No such contract shall be entered into unless the contract is fully secured by a collateralized, irrevocable letter of credit running to ERB. Cash or equivalent collateral of at least 102% of the market value of the securities plus accrued interest is 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 ERB 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. ERB may apportion income derived from the investment of cash collateral to pay its agent in securities lending transactions.

Capital Assets - Capital assets represent the cost of assets, net of accumulated depreciation, used for the administration of the Plan. Capital assets include ERB's administration building located in Santa Fe, New Mexico. ERB'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 with original cost at less than \$5,000 but categorized as sensitive, primarily IT equipment, are also capitalized for tracking and control purposes. 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.

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
 NOTES TO FINANCIAL STATEMENTS
 JUNE 30, 2014 and 2013**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Accounting Pronouncements - Governmental Accounting Standards Board (GASB) 67, *Financial Reporting for Pension Plans* and GASB 68, *Accounting & Financial Reporting for Pensions (Employer)*, address accounting and financial reporting requirements for pension plan activities. ERB is a cost-sharing multiple employer pension plan as defined by GASB 67. Changes were implemented in compliance with GASB 67 to the presentation of financial statements, notes to financial statements, and required supplementary information. ERB elected to early adopt and reflect these changes as of and for the year ended June 30, 2013. The implementation of GASB 67 did not significantly impact the accounts receivable and investment balances, as they were already accounted for in accordance with GASB 67 requirements and therefore no restatement of their 2012 balances was necessary. Implementation included the adoption of assumptions and actuarial calculation of total and net pension liability, comprehensive note disclosures regarding the assumptions and pension liability calculation, and increased investment activity disclosures.

GASB 68 applies changes implemented by GASB 67 at the employer level, segregating and allocating a portion of the Plan’s collective net pension liability to each participating employer based on their annual contributions. GASB 68 is effective for fiscal years beginning after June 15, 2014.

Net Pension Liability of Plan Membership-The components of the net pension liability of the Plan’s membership at June 30, 2014 and 2013, were as follows:

	2014	2013
Total pension liability	\$ 17,051,806,637	\$ 16,468,550,952
Plan fiduciary net position	<u>(11,346,075,824)</u>	<u>(10,191,698,803)</u>
Plan membership net pension liability	<u>\$ 5,705,730,813</u>	<u>\$ 6,276,852,149</u>
 Plan fiduciary net position as a percentage of the total pension liability	 66.54%	 61.89%

Actuarial assumptions---The total pension liability, net pension liability, and sensitivity information are based on an annual actuarial valuation performed as of June 30, 2013. The total pension liability was rolled forward from the valuation date to the Plan year ending June 30, 2014 using generally accepted actuarial principles. There were no significant events or changes in benefit provisions that required an adjustment to the roll-forward liabilities as of June 30, 2014. Specifically, the liabilities measured as of June 30, 2014 and 2013 incorporate the following assumptions:

- All members with annual salary of more than \$20,000 will contribute 10.10% during the fiscal year ending June 30, 2014 and 10.70%, thereafter,

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
 NOTES TO FINANCIAL STATEMENTS
 JUNE 30, 2014 and 2013**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

- Members hired after June 30, 2013 will have an actuarially reduced retirement benefit if they retire before age 55 and their COLA will be deferred until age 67,
- COLAs for most retirees are reduced until ERB attains a 100% funded status, and
- These assumptions were adopted by ERB on April 26, 2013 in conjunction with the six-year experience study period ending June 30, 2012.

For purposes of projecting future benefits, it is assumed that the full COLA is paid in all future years. The actuarial methods and assumptions used to determine contribution rates included in the measurement are as follows:

Actuarial Cost Method	Entry Age Normal
Amortization Method	Level Percentage of Payroll
Remaining Period	Amortized - closed 30 years from June 30, 2012 to June 30, 2042
Asset Valuation Method	5 year smoothed market
Inflation	3.00%
Salary Increases	Composition: 3% inflation, plus 1.25% productivity increase rate, plus step rate promotional increases for members with less than 10 years of service.
Investment Rate of Return	7.75%
Retirement Age	Experience based table of age and service rates.
Mortality	90% of RP-2000 Combined Mortality Table with White Collar Adjustment, projected to 2014 using Scale AA (one year setback for females)

Rate of Return: The long-term expected rate of return on pension plan investments is determined annually using a building-block approach that includes the following: 1) rate of return projections are the sum of current yield plus projected changes in price (valuation, defaults, etc.), 2) application of key economic projections (inflation, real growth, dividends, etc.), and 3) structural themes (supply and demand imbalances, capital flows, etc.). These items are developed for each major asset class.

Best estimates of geometric real rates of return for each major asset class included in the Plan's target asset allocation for 2014 and 2013 for 30-year return assumptions are summarized in the following table:

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Asset Class	2014	2013
	Long-Term Expected Real Rate of Return	Long-Term Expected Real Rate of Return
Cash	1.50%	0.75%
Treasuries	2.00%	1.00%
IG Corp Credit	3.50%	3.00%
MBS	2.25%	2.50%
Core Bonds	2.53%	2.04%
TIPS	2.50%	1.50%
High Yield Bonds	4.50%	5.00%
Bank Loans	5.00%	5.00%
Global Bonds (Unhedged)	1.25%	0.75%
Global Bonds (Hedged)	1.38%	0.93%
EMD External	5.00%	4.00%
EMD Local Currency	5.75%	5.00%
Large Cap Equities	6.25%	6.75%
Small/Mid Cap	6.25%	7.00%
International Equities (Unhedged)	7.25%	7.75%
International Equities (Hedged)	7.50%	8.00%
Emerging International Equities	9.50%	9.75%
Private Equity	8.75%	9.00%
Private Debt	8.00%	8.50%
Private Real Assets	7.75%	8.00%
Real Estate	6.25%	6.00%
Commodities	5.00%	5.00%
Hedge Funds Low Vol	5.50%	4.75%
Hedge Funds Mod Vol	5.50%	6.50%

Discount Rate-A single discount rate of 7.75% was used to measure the total pension liability as of June 30, 2014 and June 30, 2013. This single discount rate was based on the expected rate of return on pension plan investments of 7.75%. Based on the stated assumptions and the projection of cash flows, the Plan's fiduciary net position and future contributions were projected to be available to finance all projected future benefit payments of current pension plan members. Therefore the long term expected rate of return on Plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

The projection of cash flows used to determine this single discount rate assumed that Plan contributions will be made at the current statutory levels. Additionally, contributions received through the Alternative Retirement Plan (ARP) are included in the projection of cash flows. ARP contributions are assumed to remain at a level percentage of ERB payroll, where the percentage of payroll is based on the most recent five year contribution history.

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
 NOTES TO FINANCIAL STATEMENTS
 JUNE 30, 2014 and 2013**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

*Sensitivity of the net pension liability to changes in the discount rate assumption---*The following table provides the sensitivity of the net pension liability to changes in the discount rate as of June 30, 2014. In particular, the table presents the Plan’s net pension liability, if it were calculated using a single discount rate that is one-percentage-point lower (6.75%) or one-percentage-point higher (8.75%) than the single discount rate:

	1% Decrease	Current Single Rate Assumption	1% Increase
	6.75%	7.75%	8.75%
2014	\$ 7,763,304,829	\$ 5,705,730,813	\$ 3,987,098,791
2013	\$ 8,286,923,513	\$ 6,276,852,149	\$ 4,599,162,126

NOTE 2. EDUCATIONAL RETIREMENT BOARD

Plan Description—The New Mexico Educational Retirement Board (ERB) was created by the state’s Educational Retirement Act, Section 22-11-1 through 22-11-52, NMSA 1978, as amended, to administer the New Mexico Educational Employees’ Retirement Plan (Plan). The Plan is a cost-sharing, multiple employer plan established to provide retirement and disability benefits for certified teachers and other employees of the state’s public schools, institutions of higher learning, and agencies providing educational programs. The Plan is a pension trust fund of the State of New Mexico. The New Mexico legislature has the authority to set or amend contribution rates.

For the fiscal year ended June 30, 2014 employers contributed 13.15% of employees’ gross annual salary to the Educational Retirement Fund, and 10.10% of participating employees’ gross annual salary for those earning more than \$20,000. Employees earning \$20,000 or less contributed 7.90%. For fiscal year ending June 30, 2015 employers will contribute 13.90%, and employees earning more than \$20,000 will contribute 10.70% of the gross annual salary. Employees earning \$20,000 or less will continue to contribute 7.90%.

The fiscal year 2014 breakdown of public schools, institutions of higher learning, and agencies with educational programs that contribute as employers to the Plan includes the following:

Public schools	89
Universities and colleges	15
Charter schools	98
Special schools	4
State agencies	<u>24</u>
Total contributing employers	<u>230</u>

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 2. EDUCATIONAL RETIREMENT BOARD (CONTINUED)

Reporting Entity— ERB is an agency of the State of New Mexico. The Plan administered by ERB is considered part of the State financial reporting entity and is a pension trust fund of the State. The Educational Retirement Act defined a governing Board of Trustees for ERB composed of seven members (22-11-3 NMSA, 1978). The membership composition is as follows:

1. The Secretary of Public Education, or a designee of the secretary who is a resident of New Mexico; is a current employee of the Public Education Department; and possesses experience relevant to the financial or fiduciary aspects of pension or investment fund management;
2. The State Treasurer, or a designee of the Treasurer who is a resident of New Mexico; is a current employee of the State Treasurer's office; and possesses experience relevant to the financial or fiduciary aspects of pension or investment fund management;
3. One member to be elected for a term of four years by members of the New Mexico Association of Educational Retirees;
4. One member to be elected for a term of four years by the members of the National Education Association of New Mexico;
5. One member to be elected for a term of four years by the New Mexico members of the American Association of University Professors; and
6. Two members to be appointed by the governor for terms of four years each. Each member appointed shall have a background in investments, finance or pension fund administration.

The Board criteria to determine whether other state agencies, boards, or commissions that benefit the members of ERB should be included within its financial reporting entity as component units include, but are not limited to, whether ERB 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, ERB 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.

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 2. EDUCATIONAL RETIREMENT BOARD (CONTINUED)

ERB serves 230 employers in the State and has a total active, retired and inactive membership of 140,008 and 135,603 at June 30, 2014 and 2013, respectively. The following schedule shows the status and number of participants at June 30, 2014 and 2013:

	2014	2013
Retirees and beneficiaries of deceased retirees		
currently receiving benefits	42,246	39,088
Inactive members	36,589	35,304
Current active members	<u>61,173</u>	<u>61,211</u>
Total membership	<u>140,008</u>	<u>135,603</u>

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 multiplier. 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, 2010, 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 on or 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.

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 2. EDUCATIONAL RETIREMENT BOARD (CONTINUED)

- (1) *Eligibility Requirements* - To retire 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 contributions amount is the sum of the prevailing combined contributions of the member and the local administrative unit in effect at the time of the contributory employment, which was 23.25% as of June 30, 2014, 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 plus accumulated interest, determined as of the date of retirement, the balance will be paid in a lump sum to the member's surviving beneficiary.
- (3) *Benefit Options* - There are three benefit options available.

Option A – Single Life annuity - 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 member contributions plus interest less benefits paid.

Option B - The single life annuity 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. 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 single life annuity 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. 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.

- (4) *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.

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 2. EDUCATIONAL RETIREMENT BOARD (CONTINUED)

Prior to June 30, 2013 the COLA adjustment was 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, but never less than zero.

As of July 1, 2013, for current and future retirees the COLA is immediately reduced until the plan is 100% funded. The COLA reduction is based on the median retirement benefit of all retirees excluding disability retirements. Retirees with benefits at or below the median and with 25 or more years of service credit will have a 10% COLA reduction; their average COLA will be 1.8%. All other retirees will have a 20% COLA reduction; their average COLA will be 1.6%. Once the funding is greater than 90%, the COLA reductions will decrease. The retirees with benefits at or below the median and with 25 or more years of service credit will have a 5% COLA reduction; their average COLA will be 1.9%. All other retirees will have a 10% COLA reduction; their average will be 1.8%.

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.

(5) *Disability Benefit:*

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 ERB.

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 then applied.

(6) *Disability 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.

(7) The Educational Retirement Act, Section 22-11-1 to 22-11-53, NMSA 1978, assigns the authority to establish and amend benefit provisions to ERB's Board of Trustees.

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 2. EDUCATIONAL RETIREMENT BOARD (CONTINUED)

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 ERB. 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 Educational Retirement Act Sections 22-11- 47 through 52, NMSA 1978. In contrast to the defined benefit plan administered by ERB, the ARP is a defined contribution plan. Information about the ARP is provided to eligible employees by their employers, who 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. Section 22-11-47(D) allows an ARP participant the option to make an irrevocable switch to the defined benefit retirement plan after seven years of ARP participation. ARP benefits are payable in accordance with the terms of the applicable vendor contracts. Retirement benefits shall, at the option of the employee, be paid in the form of a lifetime income, if held in an annuity contract, payments for a term of years, or a single-sum cash payment. Retirement, death, and other benefits, including disability benefits, cannot be paid from the Educational Retirement Fund and ERB does not calculate or determine what benefits can be paid from an ARP account.

For the year ended June 30, 2014, colleges and universities contributed 10.15% of participating employees' gross annual salary to the ARP vendor on behalf of the participant and 3% of gross annual salary to the Educational Retirement Fund offsetting the impact of the ARP on the defined benefit plan. Employees participating in the ARP do not accrue rights to benefits in the defined benefit plan as a result of that contribution being made to the Fund.

Employer contributions include amounts remitted on behalf of the ARP defined contribution plan and the regular defined benefit plan. The 3% fee remitted to ERB for the years ended June 30, 2014 and 2013 were \$5,032,298 and \$4,684,962, respectively.

The ARP vendors are TIAA-CREF and Fidelity Investments.

NOTE 3. GENERAL FUND INVESTMENT POOL

The State General Fund Investment Pool (SGFIP) is the State of New Mexico's main operating account. State revenues such as income taxes, sales taxes, rents and royalties, and other recurring revenues are credited to the General Fund Investment Pool. The fund is comprised of numerous state agency accounts whose assets, by statute (Section 8-6-3 NMSA 1978), must be held at the State Treasury. ERB does not collect any revenues that contribute or revert to the SGFIP, but does maintain all deposits on account at the State Treasurer's Office (STO) identified by ERB's business unit and fund number.

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
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JUNE 30, 2014 and 2013**

NOTE 3. GENERAL FUND INVESTMENT POOL (CONTINUED)

In 2012 an independent diagnostic report revealed that statewide cash balances in SHARE general ledger accounts had not been reconciled to the State General Fund Investment Pool maintained at STO since the implementation of SHARE in July 2006. Since then, DFA/FCD has taken, and continues to take, aggressive action toward appropriate resolution. Phase I of the Cash Remediation Project (completed May 2013) implemented statewide business process changes and corrected numerous SHARE system configuration issues. As a result of these changes and corrections, DFA/FCD began reconciling activity reported by the State's fiscal agent bank to the SHARE general ledger on a *point forward basis* beginning February 1, 2013. However, additional critical business process changes and corrections to configuration within the SHARE system remain to be completed. Therefore, DFA/FCD has initiated Cash Management Remediation Project Phase II which is scheduled to commence shortly.

On July 11, 2014, DFA/FCD initiated the Historical Cash Reconciliation Project in partnership with Deloitte & Touche, LLP. The scope of this project is July 1, 2006 (coinciding with SHARE implementation) to January 31, 2013 (when DFA/FCD began reconciling cash activity). While this project has not been completed, preliminary results have confirmed the need to disclose that rollover cash balances associated with the General Fund Investment Pool have not been reconciled to cash accounts maintained at STO since the implementation of the SHARE system. ERB generates payments via a third party system which has not been fully reconciled to the cash account balances maintained at STO since the implementation of the SHARE system.

ERB believes cash invested in the State Treasury's Overnight Pool is represented fairly and with no material misstatements due to reconciliation procedures performed by ERB. ERB has established internal control procedures that apply the State of New Mexico Manual of Model Accounting Practices (MAP). These procedures are designed to avert accounting errors and violations of state and federal law and rules related to financial matters.

ERB uses the State's financial software general ledger system (SHARE), monitoring balances through internal reporting, and performing reconciliation procedures throughout the fiscal year, following DFA's policies and procedures for fiscal safeguards. Cash balances posted to SHARE are correct to the extent that ERB has control (i.e., collection, depositing, reconciling, and documentation of outstanding items) of the cash, its receipts and transfers to the SGFIP and other state agencies are made pursuant to DFA current policies and procedures. Each deposit, payment voucher, investment, and other items that affect cash are verified to ensure the amounts are accurate and correctly classified in the state's general ledger system.

NOTE 4. INTEREST IN THE GENERAL FUND INVESTMENT POOL

State statute (Section 8-6-3 NMSA 1978) requires ERB's cash be managed by the New Mexico State Treasurer's Office. Accordingly, ERB's investments include an interest in the General Fund Investment Pool equal to the cash balance on hand that is managed by the New Mexico State Treasurer's Office.

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013**

**NOTE 4. INTEREST IN THE GENERAL FUND INVESTMENT POOL
(CONTINUED)**

At June 30, 2014 and 2013, ERB had \$1,804,456 and \$5,353,975 respectively, invested in the General Fund Investment Pool and managed by the State Treasurer's Office.

Interest Rate Risk - The New Mexico State Treasurer's Office has an investment policy that limits investment maturities to five years or less on allowable investments. This policy manages exposure to the fair value of losses arising from increasing interest rates. This policy is reviewed and approved annually by the New Mexico State Board of Finance.

Credit risk - The New Mexico State Treasurer pools are not rated.

For additional GASB 40 disclosure information regarding cash held by the New Mexico State Treasurer, the reader should see the separate audit report for the New Mexico State Treasurer's Office for the fiscal year ended June 30, 2014.

Cash Deposits

In addition to the overnight investment at the New Mexico State Treasury, ERB invests in the Short-Term Investment Fund ("STIF"), held by J.P. Morgan. The STIF is used to facilitate more efficient trade procedures with ERB's external portfolio 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 \$275,693,396 and \$746,599,116 as of June 30, 2014 and, 2013, respectively, are considered cash equivalents and are reported as cash and short term investment balances in the statement of fiduciary net position.

Custodial Credit Risk---Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, ERB 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. ERB does not have a deposit policy for custodial credit risk. As of June 30, 2014 and 2013, 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 5. REFUND OVERPAYMENTS

In June 2010, ERB adopted a revised method for computing interest due on refunds of contributions to members that have terminated employment and elected to withdraw their contributions and on refunds paid to a beneficiary of a deceased member, with an effective date of July 1, 2010. During implementation, a programming error resulted in overpayments to 834 individuals. The total amount over paid was \$1,691,929. IRS regulations require that reasonable efforts be made to recover these funds and that interest be assessed on the overpayments. ERB accrued a receivable as of June 30, 2011 for the total amount overpaid. As of June 30, 2014, the uncollected balance, including interest assessed, was \$400,296.

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
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JUNE 30, 2014 and 2013

NOTE 6. INVESTMENTS

ERB 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.

Asset Allocation Policy---ERB's investment allocation policy is established and periodically reviewed. Allocation targets were amended on June 14, 2014. Plan assets are managed on a total return basis with the long-term objective of achieving and maintaining a fully funded status for benefits provided through the pension plan. The following schedule shows ERB's the asset allocation policy adopted on June 14, 2014 as well as the prior policy:

<u>Asset Class</u>	<u>After 6/14/2014 Target Allocation</u>	<u>Prior to 6/14/2014 Target Allocation</u>
Equities		
<i>Domestic Equities</i>		
Large cap equities	18%	20%
Small-mid cap equities	2%	2%
<i>International Equities</i>		
Developed	5%	5%
Emerging markets	<u>10%</u>	<u>10%</u>
Total Equities	<u>35%</u>	<u>37%</u>
Fixed Income		
Opportunistic credit	20%	20%
Core bonds	6%	7%
Emerging market debt	<u>2%</u>	<u>2%</u>
Total Fixed Income	<u>28%</u>	<u>29%</u>
Alternatives		
Real estate - REITS	7%	5%
Real assets	8%	7%
Private equity	11%	8%
Absolute return	0%	3%
Global tactic asset allocation	5%	5%
Risk parity	<u>5%</u>	<u>5%</u>
Total Alternatives	<u>36%</u>	<u>33%</u>
Cash	<u>1%</u>	<u>1%</u>
Total	<u>100%</u>	<u>100%</u>

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
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NOTE 6. INVESTMENTS (CONTINUED)

Rate of Return---For the year ended June 30, 2014, the annual money-weighted rate of return on pension plan investments, net of pension plan investment expense, was 14.71%. For the year ended June 30, 2013, the annual money-weighted rate of return on pension plan investments, net of pension plan investment expense, was 11.12%. The money-weighted rate of return expresses investment performance, net of investment expense, adjusted for the changing amounts actually invested.

Investments held by ERB's agent in the name of ERB as of June 30:

Investment Description:	2014	2013
U.S. government and agency securities	\$ 470,995,039	\$ 572,532,940
Non-U.S. government bonds	134,285,504	109,518,808
Asset-and mortgage-backed securities	660,105,257	692,017,167
Non-U.S. asset-backed securities	53,344,875	22,740,459
Domestic corporate bonds	803,363,210	757,378,340
Non-U.S. corporate bonds	253,934,520	245,228,240
Domestic stocks	2,894,639,685	2,824,846,950
International stocks	1,985,766,369	1,134,562,079
Hedge funds of funds	631,121,208	463,853,968
Private equity	850,638,967	670,818,353
Private real estate	270,577,050	199,274,198
Infrastructure	132,824,443	116,052,810
Natural resources	91,618,965	48,890,160
Other investments	<u>1,793,076,832</u>	<u>1,581,574,828</u>
Total	<u>\$ 11,026,291,924</u>	<u>\$ 9,439,289,300</u>

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 6. 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 ERB's investment in foreign equity securities. Managers of these assets are given discretion to hedge this risk. ERB's exposure to foreign currency risk was \$897,957,814 and \$1,451,831,846 as of June 30, 2014 and 2013, respectively.

As of June 30, 2014, exposure to foreign currency risk by type is as follows:

Currency	Equity Securities	Cash (overdraft)
Australian Dollar	\$ 23,077,159	\$ 3,317,644
Brazilian Real	41,050,490	55,677
British Pound Sterling	87,004,051	4,191,242
Canadian Dollar	1,790,449	110,833
Chilean Peso	204,866	-
Chinese Yuan	(21,691)	-
Chinese Yuan Renminbi (offshore)	4,572	-
Colombian Peso	3,678,401	-
Czech Koruna	676,774	(3,677)
Danish Krone	5,054,160	-
Euro	219,461,000	(15,493,648)
Hong Kong Dollar	85,222,886	239,776
Hungarian Forint	7,520,755	(1,178,604)
Indian Rupee	41,767,803	41,531
Indonesian Rupiah	15,322,840	(2,692)
Israeli Shekel	1,643,785	-
Japanese Yen	55,059,307	46,343
Malaysian Ringgit	15,631,346	-
Mexican Peso	20,398,514	48
Romanian Leu, New	2,668,978	-
Taiwan Dollar, New	51,547,278	104,930
Turkish Lira, New	23,594,599	15,139
New Zealand Dollar	-	1,825
Nigerian Naira	2,044,615	-
Norwegian Krone	1,595,678	33,989
Peruvian Nuevo Sol	1,880,926	-
Philippine Peso	935,542	-
Polish Zloty	9,790,428	2,463
Qatari Riyal	1,663,502	-
Russian Ruble	9,943,706	1,685,655
Singapore Dollar	7,271,795	3,579
South African Rand	39,150,858	(37,118)
South Korean Won	84,116,875	139
Swedish Krona	9,229,267	-
Swiss Franc	23,410,496	(189,900)
Thai Baht	11,620,628	-
Total foreign exposure	905,012,640	(7,054,826)
Investments not subject to foreign currency risk	10,121,279,284	282,748,220
Total Investments	<u>\$ 11,026,291,924</u>	<u>\$ 275,693,394</u>

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 6. INVESTMENTS (CONTINUED)

As of June 30, 2013 exposure to foreign currency risk is as follows:

Currency	Equity Securities	Cash (overdraft)
Australian Dollar	\$ 31,982,137	\$ 153,383
Brazilian Real	76,289,449	243,540
British Pound Sterling	140,848,446	(5,968,354)
Canadian Dollar	3,457,884	328,511
Chilean Peso	247,115	-
Chinese Yuan Renminbi (offshore)	19,030	-
Colombian Peso	2,678,948	-
Czech Koruna	4,796,272	52,531
Danish Krone	5,690,398	(14,859)
Euro	268,885,759	7,362,938
Hong Kong Dollar	181,672,431	2,751,963
Hungarian Forint	11,039,091	155,500
Indian Rupee	58,565,752	370,029
Indonesian Rupiah	33,443,062	54
Israeli Shekel	2,092,366	11,285
Japanese Yen	113,834,989	7,787
Malaysian Ringgit	16,253,070	-
Mexican Peso	19,059,786	133,195
Romanian Leu, New	708,909	-
Taiwan Dollar, New	54,219,803	1,416,346
Turkish Lira, New	47,101,447	55,644
New Zealand Dollar	-	1,610
Nigerian Naira	2,797,236	-
Norwegian Krone	5,448,046	(85,750)
Peruvian Nuevo Sol	2,332,307	-
Philippine Peso	1,358,743	-
Polish Zloty	22,538,302	60,114
Qatari Riyal	-	-
Russian Ruble	13,487,050	143,826
Singapore Dollar	12,625,599	58,568
South African Rand	45,724,796	171,001
South Korean Won	174,895,731	133
Swedish Krona	9,723,172	67,237
Swiss Franc	43,407,409	33,512
Thai Baht	37,097,566	-
Total foreign exposure	1,444,322,101	7,509,744
Investments not subject to foreign currency risk	7,994,967,199	739,089,372
Total Investments	<u>\$ 9,439,289,300</u>	<u>\$ 746,599,116</u>

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013**

NOTE 6. INVESTMENTS (CONTINUED)

Custodial Credit Risk—Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty, ERB will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. Based on ERB’s investment policies and custody agreements, ERB has determined its custody risk is very low.

All investments were held by J.P. Morgan (Dallas, Texas) during fiscal years 2014 and 2013 in the name of ERB. During fiscal year 2015 investments will be transferred to State Street (Boston, Massachusetts) to be held in custody for ERB.

ERB’s investment policy limits holding of securities by counterparties to those involved with securities lending. In 2012, ERB ended its practice of securities lending.

Interest Rate Risk—Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. ERB 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. ERB uses the weighted average method to determine the duration of its investments.

As of June 30, 2014, ERB’s exposure to interest rate risk is summarized below.

Investment Type	2014	2013	Duration (In Years)	
			2014	2013
U.S. treasury securities	\$ 328,169,191	\$ 276,356,253	5.83	6.05
U.S. government & government related obligations	53,982,302	62,066,857	3.47	6.17
International government Obligations	58,451,211	61,262,317	5.61	5.48
Corporate obligations	1,025,740,824	1,035,566,130	2.95	4.03
Asset- & mortgage-backed sec.	174,130,475	378,794,011	1.30	756
Short term investments	<u>60,069,681</u>	<u>124,396,288</u>	0.02	0.01
Overall	<u>\$1,700,543,684</u>	<u>\$1,938,441,856</u>	3.75	3.68

Credit Risk—Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. 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, ERB’s credit quality distribution for investments with credit risk exposure as of June 30, 2014 and 2013, is presented in the Summary of Investment by Rating. The investments were rated and categorized according to Standard & Poor’s rating standards.

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 6. INVESTMENTS (CONTINUED)

Summary by Credit Risk Rating		2014		2013	
Investment Type	Rating	Fair Value	Rating	Fair Value	
Asset Backed Securities	A	\$ 2,550,282	A	\$ -	
	A-	854,815	A-	326,704	
	A+	195,539	A+	3,396,227	
	AA-	-	AA-	2,752,095	
	AA+	1,378,301	AA+	1,373,085	
	AAA	2,381,679	AAA	1,166,787	
	B	-	B	1,475,147	
	B-	612,869	B-	726,309	
	B+	-	B+	843,752	
	BB	-	BB	625,056	
	BB-	-	BB-	2,803,920	
	BB+	877,807	BB+	1,646,159	
	BBB	631,958	BBB	-	
	BBB-	239,610	BBB-	754,798	
	BBB+	769,620	BBB+	3,508,673	
	CC	20,746	CC	4,541	
	CCC	1,540,467	CCC	2,914,298	
	CCC-	407,060	CCC-	526,249	
	D	251	D	370,349	
	NR	3,748,066	NR	10,731,333	
Sub Total Asset Backed Securities		<u>16,209,069</u>		<u>35,945,482</u>	
Commercial Mortgage Backed-REMIC	A	3,299,452	A	4,272,389	
	A-	509,665	A-	2,069,348	
	A+	4,390,579	A+	6,462,388	
	AA	5,001,021	AA	4,951,201	
	AA-	-	AA-	1,734,784	
	AA+	834,653	AA+	25,172,635	
	AAA	4,339,622	AAA	20,849,127	
	B	514,213	B	774,283	
	B-	458,215	B-	-	
	B+	829,051	B+	-	
	BB	54,391	BB	890,377	
	BB-	-	BB-	483,384	
	BB+	173,577	BB+	465,894	
	BBB	-	BBB	3,248,428	
	BBB-	8,627,366	BBB-	9,930,636	
	BBB+	11,761,347	BBB+	15,858,641	
	CC	-	CC	1,193,566	
	CCC	674,453	CCC	4,117,344	
	CCC+	226,626	CCC+	-	
	D	842,095	D	5,046,012	
	NR	8,173,049	NR	8,960,300	
Subtotal Commercial Mortgage Backed Securities		<u>60,709,376</u>		<u>116,480,737</u>	
Mortgage Backed Securities	AA+	22,521,250	AA+	205,715,824	
Residential Mortgage Backed Security	CCC	3,363,806	CCC	-	
Total Asset & Mortgage Backed Securities		<u>\$ 202,803,501</u>		<u>\$358,142,043</u>	

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 6. INVESTMENTS (CONTINUED)

Summary by Credit Risk Rating Continued		2014		2013	
Investment Type	Rating	Fair Value	Rating	Fair Value	
Collateralized Debt-Loan Obligations	AA-	\$ 2,835,345	AA-	\$ -	
	B	1,664,100	B	-	
	B-	645,737	B-	-	
	BB	730,232	BB	-	
	BB+	2,213,050	BB+	-	
	BBB+	474,071	BBB+	-	
	CCC+	728,997	CCC+	-	
	NR	1,851,184	NR	-	
	Subtotal Collateralized Debt-Loan Obligations		<u>11,142,716</u>		<u>-</u>
Collateralized Mortgage Obligation/REMIC	A+	565,209	A+	-	
	AA+	836,513	AA+	-	
	AAA	1,970,250	AAA	-	
	B	675,894	B	-	
	BBB	1,025,729	BBB	-	
	BBB-	1,337,587	BBB-	-	
	BBB+	581,623	BBB+	-	
	CC	846,772	CC	-	
	CCC	966,135	CCC	-	
	D	2,194,884	D	-	
	NR	1,087,526	NR	-	
Subtotal Collateralized Mortgage Obligation/REMIC		<u>12,088,123</u>		<u>-</u>	
Total Collateralized Debt Obligations		<u>\$ 23,230,839</u>		<u>\$ -</u>	

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 6. INVESTMENTS (CONTINUED)

Summary by Credit Risk Rating Continued		2014		2013	
Investment Type	Rating	Fair Value	Rating	Fair Value	
Corporate Bonds	A	\$ 35,525,907	A	\$ 41,111,424	
	A-	73,579,414	A-	75,261,961	
	A+	13,581,147	A+	14,506,159	
	AA	2,850,945	AA	4,762,359	
	AA-	7,577,036	AA-	9,051,938	
	AA+	4,917,261	AA+	7,068,655	
	AAA	373,031	AAA	346,441	
	B	14,610,140	B	53,906,046	
	B-	58,470,962	B-	81,556,774	
	B+	8,408,611	B+	19,718,930	
	BB	1,565,433	BB	5,464,875	
	BB-	2,624,787	BB-	1,574,050	
	BB+	12,155,066	BB+	8,870,611	
	BBB	69,839,101	BBB	83,111,389	
	BBB-	58,488,780	BBB-	53,644,216	
	BBB+	69,048,894	BBB+	54,296,843	
	C	2,969,250	C	1,276,843	
	CC	571,200	CC	4,273,315	
	CCC	15,971,976	CCC	23,169,923	
	CCC-	25,730,506	CCC-	23,869,704	
CCC+	42,867,696	CCC+	87,221,268		
D	8,180,217	D	3,000,820		
NR	102,262,848	NR	124,050,538		
Subtotal Corporate Bonds		<u>632,170,208</u>		<u>781,115,082</u>	
Corporate Convertible Bonds	NR	13,631,012	NR	12,581	
Common Stock	NR	92,993,837	NR	60,019,213	
Preferred Stock	D	730,209	D	-	
	NR	4,304,468	NR	31	
Subtotal Preferred Stock		<u>5,034,677</u>		<u>15,031</u>	
Total Domestic Corporate Securities		<u>\$ 743,829,734</u>		<u>\$ 841,161,907</u>	

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 6. INVESTMENTS (CONTINUED)

Summary by Credit Risk Rating Cont		2014		2013	
Investment Type	Rating	Fair Value	Rating	Fair Value	
Bank Loans	B	\$ 7,174,861	B	\$ 22,271,989	
	B-	14,868,320	B-	25,129,006	
	B+	14,210,746	B+	7,399,821	
	BB-	(110,712)	BB-	-	
	CCC	10,696,722	CCC	16,730,614	
	CCC-	6,807,880	CCC-	-	
	CCC+	25,748,680	CCC+	17,394,221	
	D	14,819,805	D	-	
	NR	174,109,344	NR	61,994,639	
Subtotal Bank Loans		<u>268,325,647</u>		<u>150,920,290</u>	
Municipal & Provincial Bonds	A	2,258,611	A	5,790,728	
	A-	6,230,958	A-	4,048,878	
	A+	2,252,107	A+	84,012	
	AA	1,545,951	AA	-	
	AA-	991,191	AA-	-	
	AA+	199,264	AA+	-	
Subtotal Government Agencies		<u>13,478,081</u>		<u>9,923,618</u>	
Government Bonds	A	25,111,778	A	8,520,138	
	A-	10,510,943	A-	37,227,454	
	A+	-	A+	837,154	
	AA-	3,429,431	AA-	3,978,722	
	AA+	21,579,345	AA+	25,587,621	
	AAA	622,139	AAA	2,821,180	
	B-	294,000	B-	-	
	BB	7,511,959	BB	5,992,772	
	BB+	1,312,986	BB+	-	
	BBB	12,152,394	BBB	3,065,909	
	BBB-	3,638,845	BBB-	1,314,939	
	BBB+	19,951,968	BBB+	8,860,780	
	NR	52,124,417	NR	38,215,442	
Subtotal Government Bonds		<u>158,240,206</u>		<u>136,422,111</u>	
Treasury Bills	BBB+	398,297	BBB+	-	
	NR	857,813	NR	-	
Subtotal Treasury Bills		<u>1,256,111</u>		<u>-</u>	
Other Fixed Income	B-	9,241,025	B-	-	
	BB+	2,072,892	BB+	-	
	NR	9,190,422	NR	4,707,917	
Subtotal Other Investments		<u>20,504,339</u>		<u>4,707,917</u>	
Other Investments Not Subject To Credit Risk		<u>9,594,623,466</u>		<u>7,938,011,414</u>	
Grand Total		<u>\$ 11,026,291,923</u>		<u>\$ 9,439,289,300</u>	

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 6. INVESTMENTS (CONTINUED)

Cash Balances —ERB 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, ERB’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 5% or more of the pension plan’s fiduciary net position. As of June 30, 2014 and 2013, with the exception of U.S. government and agency securities, ERB was not exposed to any concentration risk greater than 5%.

NOTE 7. DERIVATIVE INSTRUMENTS

Derivatives are generally defined as contracts or securities whose value depend on, or derive from, the value of an underlying asset, reference rate, or index.

ERB has adopted GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, which addresses the recognition, measurement, and disclosure of derivative instruments. This note describes ERB’s investment derivative instruments measured at fair value in the Statement of Fiduciary Net Position and Statement of Changes in Fiduciary Net Position.

ERB’s investment policies do allow for certain portfolio managers to trade in certain derivatives for hedging purposes

The notional or contractual amounts of derivatives indicate the extent of ERB’s involvement in the various types and uses of derivative financial instruments and do not measure ERB’s exposure to credit or market risks and do not necessarily represent amounts exchanged by the parties. The amounts exchanged are determined by reference to the notional amounts and other terms of the derivatives.

The following table summarizes the aggregate notional or contractual amounts for ERB’s derivative financial instruments as of June 30, 2014 and 2013.

Instrument	Notional Amounts	
	2014	2013
Futures contracts - long	\$ 1,043,000	\$ 4,430,000
Futures contracts - short	37,743,000	(15,500,000)
Foreign exchange forward contracts, net	200,722,000	403,280,000
Swaps - credit default swap	1,870,000	7,870,000
Swaps - index swap	227,000	284,000

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 7. DERIVATIVE INSTRUMENTS (CONTINUED)

The fair values of derivative instruments outstanding as of June 30, 2014 and 2013 are classified by type and by the changes in fair value of the derivative instrument in the following table.

Derivative Type	Classification	Fair Value at June 30, 2014		
		Gain/(Loss)	Classification	Amount
Futures	Investment Income	\$ (216,000)	Investment	\$(304,000)
Options - purchased	Investment Income	9,000	Investment	9,000
Options - sold	Investment Income	(15,000)	Investment	(15,000)
Swaps - Credit Default Swap Index	Investment Income	(51,000)	Investment	24,000
Swaps - Interest Rate Swaps	Investment Income	(6,000)	Investment	23,000
Swaps - Index	Investment Income	-	Investment	29,000

Derivative Type	Classification	Fair Value at June 30, 2013		
		Gain/(Loss)	Classification	Amount
Futures	Investment Income	\$ 14,000	Investment	\$ (87,000)
Options - purchased	Investment Income	6,000	Investment	-
Options - sold	Investment Income	141,000	Investment	-
Swaps - Credit Default Swap Index	Investment Income	183,000	Investment	76,000
Swaps - Interest Rate Swaps	Investment Income	21,000	Investment	-
Swaps - Index	Investment Income	12,000	Investment	29,000

Risks--- There are certain risks inherent in investments in derivatives. ERB is exposed to credit risk in the event of non-performance by counterparties to financial instruments. The fund managers that are authorized to invest in derivatives are given specific parameters as to the types of derivatives invested in and ratings of the counterparties they are allowed to enter into contracts with to ensure transactions are entered into with only high quality institutions. ERB is exposed to market risk; the risk that changes in market conditions may make an investment less valuable. Exposure to market risk is managed within risk limits set by management through buying and selling of specific instruments or by entering into offsetting positions. As discussed in note 6, foreign currency risk for investments is the risk that changes in exchange rates will adversely affect the investments. Managers of these assets are given discretion to hedge this risk.

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 7. DERIVATIVE INSTRUMENTS (CONTINUED)

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 ERB'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. The following tables summarize the ERB's foreign exchange contracts by currency as of June 30, 2014 and 2013.

Summary of Foreign Exchange Contracts by Currency
Fiscal Year Ending June 30, 2014

Currency	Buys	Unrealized Gain/(Loss)	Sells	Unrealized Gain/(Loss)
Australian Dollar	-	88,000	-	(99,374)
Brazilian Real	20,964,000	230,000	-	(247,220)
British Pound Sterling	-	-	44,148,957	(24,123)
Canadian Dollar	-	3,000	-	(27,255)
Chilean Peso	775,000,000	11,000	-	(41,318)
Colombian Peso	27,400,000	(62,000)	813,000,000	20,971
Euro	7,605,303,000	86,000	6,500,000	(46,801)
Hungarian Forint	1,378,000	22,000	4,373,202,348	164,170
Indian Rupee	500,175,000	118,000	-	31,714
Indonesian Rupiah	213,300,000	(36,000)	507,971,281	(616)
Japanese Yen	7,700,000,000	(19,000)	101,000,000	45,692
Malaysian Ringgit	-	361,000	19,076,928,115	(116,057)
Mexican Peso	5,431,000	22,000	-	(358)
Romanian Leu, New	75,215,000	383,000	530,338	(418,848)
Taiwan Dollar, New	1,168,000	9,000	15,892,914	(3,821)
Turkish Lira, New	-	5,000	2,023,802	(4,652)
Peruvian Nuevo Sol	8,453,000	45,000	-	(29,944)
Philippine Peso	594,000	(2,000)	8,536,143	(2,155)
Polish Zloty	19,152,000	76,000	-	(119,739)
Russian Ruble	9,555,000	25,000	16,700,000	(27,381)
Singapore Dollar	52,067,000	92,000	3,156,846	(592,657)
South African Rand	-	47,000	201,968,139	(111,306)
South Korean Won	14,958,000	(3,000)	4,700,000	2,123
Swiss Franc	-	74,000	23,032,372	(70,376)
Thai Baht	-	-	1,607,511	(12,539)
US Dollar	30,591,000	5,000	38,600,000	3,072
Total	52,013,000	-	48,065,216	-
	<u>\$ 17,112,717,000</u>	<u>\$ 1,580,000</u>	<u>\$ 25,287,563,982</u>	<u>\$ (1,728,798)</u>

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 7. DERIVATIVE INSTRUMENTS (CONTINUED)

Summary of Foreign Exchange Contracts by Currency
Fiscal Year Ending June 30, 2013

Currency	Buys	Unrealized Gain/(Loss)	Sells	Unrealized Gain/(Loss)
Australian Dollar	\$ 3,205,000	\$ (96,000)	\$ 3,146,000	\$ 390,000
Brazilian Real	5,734,000	(209,000)	3,617,000	144,000
British Pound Sterling	-	-	5,589,000	22,000
Canadian Dollar	275,000	(3,000)	1,917,000	49,000
Chilean Peso	825,000	(3,000)	1,639,000	21,000
Chinese Yuan Renminbi	1,164,000	32,000	1,165,000	(22,000)
Colombian Peso	1,178,000	(72,000)	-	46,000
Euro	3,091,000	(50,000)	39,029,000	(17,000)
Hungarian Forint	6,206,000	(114,000)	6,530,000	28,000
Indian Rupee	-	(1,000)	-	1,000
Indonesian Rupiah	-	(5,000)	1,646,000	(6,000)
Japanese Yen	9,836,000	(361,000)	9,876,000	113,000
Malaysian Ringgit	184,000	(8,000)	-	-
Mexican Peso	18,153,000	(514,000)	12,248,000	424,000
Romanian Leu, New	429,000	(7,000)	-	-
Taiwan Dollar, New	1,555,000	(5,000)	1,528,000	6,000
Turkish Lira, New	3,017,000	(42,000)	-	72,000
Peruvian Nuevo Sol	-	-	239,000	2,000
Philippine Peso	2,266,000	(68,000)	3,151,000	143,000
Polish Zloty	3,867,000	(44,000)	814,000	68,000
Russian Ruble	6,834,000	(114,000)	10,980,000	458,000
Singapore Dollar	4,299,000	(67,000)	5,035,000	111,000
South African Rand	4,155,000	(53,000)	4,259,000	16,000
South Korean Won	6,794,000	(74,000)	6,794,000	121,000
Thai Baht	-	7,000	1,738,000	(5,000)
US Dollar	118,483,000	-	80,788,000	-
Total	\$ 201,550,000	\$(1,871,000)	\$ 201,728,000	\$ 2,185,000

Futures Contracts—ERB 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 Statement of Fiduciary Net Position. The credit risk associated with these contracts is minimal as they are traded on organized exchanges and settled daily.

During 2014 and 2013, ERB 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, ERB 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.

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 7. DERIVATIVE INSTRUMENTS (CONTINUED)

Subsequent payments are then made or received by the ERB, depending on the daily fluctuation in the value of the underlying contracts. Cash Collateral in the amount of \$750,061 as of June 30, 2014 was held in a Money Market fund by the custodial bank. U.S. Treasury Securities owned and included in the investments of the ERB, with a value of approximately \$1,800,000 as of June 30, 2013 were held by the Plan's broker as performance security on futures contracts.

2014		
Summary of Outstanding Futures Contracts		
	No. of Contracts	Notional Amount
Futures Contracts - Long	148	\$ 1,052,500
Futures Contracts - Short	509	\$ 37,742,500
		Fair Value
Margin Deposit		\$ 750,061

2013		
Summary of Outstanding Futures Contracts		
	No. of Contracts	Notional Amount
Futures Contracts - Long	134	\$ 4,430,000
Futures Contracts - Short	107	\$ 15,500,000
		Fair Value
Margin Deposit		\$ 1,800,000

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 of a designated instrument at a specified price within a specified period of time. When ERB 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, 2014 and June 30, 2013, there were no open written or purchased options.

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 7. DERIVATIVE INSTRUMENTS (CONTINUED)

Swap Contracts — Swap contracts are executed on a number of different bases. The two types employed by ERB on June 30, 2014 and June 30 2013, were interest rate swap contracts and credit default swap contracts. 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. 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--- The use of other derivatives is allowed under the Hedge Fund Investment Policy. These investments are under the management of the Hedge Fund managers who are employed in the “Hedge Fund”, “Emerging Market Debt” and “Opportunistic Credit” classifications.

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. The securities are held for investment purposes. The assets are as follows:

Investment	2014	2013
Asset Backed Securities	\$ 17,759,591	\$ 18,862,108
Collateralized Debt Obligations	12,154,510	41,616,321
Commercial Mortgage-Backed /REMIC	62,957,532	76,699,558
Collateralized Mortgage Obligation/REMIC	11,142,716	19,149,599
	<u>\$ 104,014,349</u>	<u>\$ 156,327,586</u>

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 8. CAPITAL ASSETS

Capital assets relate to all assets of ERB that are used in operations and have useful lives extending beyond a single reporting period. Depreciation expense was \$168,880 and \$695,347 for the years ended 2014 and 2013, respectively. Capital asset activity for the years ended June 30, 2014 and 2013 is as follows:

	Beginning Balance	Additions	Deletions	Ending Balance
2014:				
Land	\$ 248,172	\$ -	\$ -	\$ 248,172
Depreciable land improvements	19,361	-	-	19,361
Building and building improvements	3,365,714	-	-	3,365,714
Furniture and equipment	1,082,574	-	23,425	1,059,149
Other assets (Art in Public Places)	30,500	-	-	30,500
Integrated Retirement Information System (IRIS)	9,156,963	21,548	62,602	9,115,909
Total	13,903,284	21,548	86,027	13,838,805
Accumulated depreciation:				
Depreciable land improvements	5,721	1,322	-	7,043
Building and building improvements	1,616,025	101,211	-	1,717,236
Furniture and equipment	948,798	8,398	21,830	935,366
Integrated Retirement Information System (IRIS)	9,156,963	57,949	64,381	9,150,531
Total	11,727,507	168,880	86,211	11,810,176
Capital assets—net	\$ 2,175,777	\$ (147,332)	\$ (183)	\$ 2,028,629

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 8. CAPITAL ASSETS (CONTINUED)

	Beginning Balance	Additions	Deletions	Ending Balance
2013:				
Land	\$ 248,172	\$ -	\$ -	\$ 248,172
Depreciable land improvements	19,361	-	-	19,361
Building and building improvements	3,365,714	-	-	3,365,714
Furniture and equipment	1,124,917	8,496	50,839	1,082,574
Other assets (Art in Public Places)	30,500	-	-	30,500
Integrated Retirement Information System (IRIS)	9,156,963	-	-	9,156,963
Total	13,945,627	8,496	50,839	13,903,284
Accumulated depreciation:				
Depreciable land improvements	5,022	699	-	5,721
Building and building improvements	1,514,134	101,891	-	1,616,025
Furniture and equipment	912,815	86,704	50,721	948,798
Integrated Retirement Information System (IRIS)	8,650,910	506,053	-	9,156,963
Total	11,082,881	695,347	50,721	11,727,507
Capital assets—net	\$ 2,862,746	\$ (686,851)	\$ 118	\$ 2,175,777

NOTE 9. RETIREMENT PLANS

ERB employees 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 ERB employees have elected to participate in the Educational Employees' Retirement Plan (ERB Plan) through the Educational Retirement Act, while most employees have elected to participate in the Public Employees Retirement Plan (PERA Plan).

Public Employees Retirement Association (PERA). Certain full-time employees elect to participate in the PERA Plan authorized under the Public Employees Retirement Act (Chapter 10, Article 11, NMSA 1978). The Public Employees Retirement Association (PERA) is the administrator of the PERA 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 PERA 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.

PERA announced on September 10, 2014 that the agency will implement GASB 67 in their fiscal year 2014 financial report. The total collective pension liability will then be allocated to participant employers for fiscal year 2015 reporting. The Schedule of Employer Allocations

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 9. RETIREMENT PLANS (CONTINUED)

will be provided to employers, including ERB, in April 2015, allowing enough time for incorporation into ERB's fiscal year 2015 financial report as required by GASB 68.

PERA Funding Policy. Plan members are required to contribute 8.92% of their gross salary. ERB is required to contribute 16.99% of the gross covered salary. The contribution requirements of plan members and ERB are established in State statute under Chapter 10, Article 11, NMSA 1978. The requirements may be amended by acts of the legislature. Total contributions from ERB and Plan members to PERA for the fiscal years ending June 30, 2014 and 2013, and 2012 were \$709,380, \$656,229, and \$661,881, 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 ERB is the administrator of the ERB 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 ERB 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.

ERB Funding Policy.

Member Contributions

Plan members whose annual salary is \$20,000 or less are required by statute to contribute 7.9% of their gross salary. Plan members whose annual salary is over \$20,000 are required to make the following contributions to the Plan: 9.4% of their gross salary in fiscal year 2013; 10.1% of their gross salary in fiscal year 2014; and 10.7% of their gross salary in fiscal year 2015 and thereafter.

Employer Contributions

ERB contributed 13.15% of gross covered employee salaries in fiscal year 2014. Contributions will be 13.9% of gross covered salary in fiscal year 2015.

In fiscal year 2013, ERB was required to contribute 12.4% of the gross covered salary for employees whose annual salary was \$20,000 or less, and 10.9% of the gross covered salary for employees whose annual salary was more than \$20,000.

The contribution requirements of Plan members and ERB are established in State statute under Chapter 22, Article 11, NMSA 1978. The requirements may be amended by acts of the legislature. ERB's contributions to the Plan for the fiscal years ending June 30, 2014 and 2013 were \$2,623 and \$7,190 respectively, which equal the amount of the required contributions for each fiscal year.

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014 and 2013

NOTE 10. POST-EMPLOYMENT BENEFITS – STATE RETIREE HEALTH CARE PLAN

Plan Description: ERB contributes to the New Mexico Retiree Health Care Fund, a cost-sharing multi-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). RHCA 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 legislators who served at least two years; (4) former governing authority members who served at least four years.

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.

Funding Policy. The Retiree Health Care Act (Section 10-7C-13, NMSA 1978) authorizes RHCA 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 RHCA Plan. The monthly premium rate schedule can be obtained from the RHCA or viewed on their website at www.nmrhca.state.nm.us.

The employer, employee and retiree contributions are required to be remitted to RHCA on a monthly basis. The statutory requirements for the employer and employee contributions can be changed by the New Mexico State Legislature. Employers that choose to become participating employers after January 1, 1998, are required to make contributions to the RHCA fund in the amount determined to be appropriate by RHCA.

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
 NOTES TO FINANCIAL STATEMENTS
 JUNE 30, 2014 and 2013**

NOTE 10. POST-EMPLOYMENT BENEFITS-STATE RETIREE HEALTH CARE PLAN (CONTINUED)

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. For employees that were members of an enhanced retirement PERA plan (state police and adult correctional officer member coverage plan 1; municipal police member coverage plans 3, 4 or 5; municipal fire member coverage plan 3, 4 or 5; municipal detention officer member coverage plan 1; and members pursuant to the Judicial Retirement Act) during the fiscal year ended June 30, 2013, the statute required each participating employer to contribute 2.5% of each participating employee’s annual salary; and each participating employee was required to contribute 1.25% of their salary. For employees that were not members of an enhanced retirement PERA Plan during the fiscal year ended June 30, 2013, the statute required each participating employer to contribute 2.0% of each participating employee’s annual salary; each participating employee was required to contribute 1.0% of their salary.

In addition, pursuant to Section 10-7C-15(G) NMSA 1978, at the first session of the Legislature following July 1, 2013, the legislature shall review and adjust the distributions pursuant to Section 7-1-6.1 NMSA 1978 and the employer and employee contributions to the authority in order to ensure the actuarial soundness of the benefits provided under the Retiree Health Care Act.

ERB’s contributions to the RHCA for the years ending June 30, 2014 and 2013 were \$56,618 and \$55,678 for employer contributions and \$36,915 and \$27,836 in employee contributions, respectively, which equal the required contributions for each year.

NOTE 11. RISK MANAGEMENT

With the exception of investment losses, ERB 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, ERB is responsible for only a small deductible payment in amounts that vary according to the type of claim.

NOTE 12. STATUTORY DISCLOSURES

Section 2.2.2.10P(2) of the Audit Rule 2011, 2.2.2 NMAC entitled, “Requirements for Contracting and Conducting Audits of Agencies” requires that state agencies disclose all special, deficiency, and specific appropriations. ERB received the following specific appropriations:

IRIS ENHANCEMENT PROJECT

Laws of 2011, Chapter 179, Section 7, Item 3

Appropriation	\$ 3,500,000
Expended FY 2012 to 2014	(3,452,901)
Outstanding Encumbrance at end of FY 2014	-
Un-encumbered balance for FY2015	<u>\$ 47,099</u>

REQUIRED SUPPLEMENTARY INFORMATION

**STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF CHANGES IN THE EMPLOYERS' NET PENSION LIABILITY**

(Unaudited)

Fiscal year ending June 30,

	2014	2013
Total Pension Liability		
Service Cost	\$ 350,247,724	\$ 348,266,697
Interest	1,254,730,237	1,202,676,449
Benefit Changes	-	10,093,494
Difference between actual & expected experience	(114,507,809)	-
Assumption Changes	-	(5,035,689,829)
Benefit Payments	(868,291,384)	(811,665,051)
Refunds	(38,923,083)	(41,664,216)
Net Change in Total Pension Liability	\$ 583,255,685	\$ (4,327,982,456)
Total Pension Liability - Beginning	16,468,550,952	20,796,533,408
Total Pension Liability - Ending (a)	\$ 17,051,806,637	\$ 16,468,550,952
Plan Fiduciary Net Position		
Contributions - Employer	\$ 362,462,537	\$ 299,657,530
Contributions - Member	268,693,991	250,529,546
Net Investment Income	1,444,688,793	1,016,865,792
Benefit Payments	(865,471,799)	(811,665,051)
Refunds	(38,923,083)	(41,664,216)
Administrative Expense	(16,611,673)	(10,985,967)
Net Change in Plan Fiduciary Net Position	\$ 1,154,838,766	\$ 702,737,634
Plan Fiduciary Net Position - Beginning	10,191,698,803	9,488,961,169
Plan Fiduciary Net Position - Ending (b)	\$ 11,346,537,569	\$ 10,191,698,803
Net Pension Liability - Ending (a) - (b)	\$ 5,705,269,068	\$ 6,276,852,149
Plan fiduciary Net Position as a Percentage of Total Pension Liability	66.54%	61.89%
Covered Employee Payroll	\$ 2,718,100,677	\$ 2,706,170,349
Net Pension Liability as a Percentage of Covered Employee Payroll	209.92%	231.95%

Notes to Schedule:

*The change in total pension liability due to assumption changes for the fiscal year ending June 30, 2013 includes the impact of the new assumptions adopted by the Board on April 26, 2013 as well as the change in the single discount rate between June 30, 2012 and June 30, 2013.

*The covered employee payroll is the actual payroll, reported from the total employer contribution for the fiscal year ending June 30.

**STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF THE NET PENSION LIABILITY**

(Unaudited)

Fiscal year ending June 30,

	2014	2013
Total Pension Liability	\$ 17,051,806,637	\$ 16,468,550,952
Plan Fiduciary Net Position	11,346,075,824	10,191,698,803
Net Pension Liability	<u>\$ 5,705,730,813</u>	<u>\$ 6,276,852,149</u>
 Plan Fiduciary Net Position as a Percentage of a Total Pension Liability	 66.54%	 61.89%
 Covered Employee Payroll	 \$ 2,718,100,677	 \$ 2,706,170,349
 Net Pension Liability as a Percentage of Covered Employee Payroll	 209.92%	 231.95%

**STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF INVESTMENT RETURNS**

(Unaudited)

<u>FY Ending June 30</u>	<u>Annual Money-Weighted Rate of Return, Net of Investment Expense</u>
2014	14.71%
2013	11.12%
2012	1.87%
2011	19.30%

**STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF EMPLOYER CONTRIBUTIONS**

(Unaudited)

FY Ending June 30	Actuarially Determined Contribution	Actual Contribution	Contribution Deficiency (Excess)	Covered Payroll	Contribution as a % of Covered Payroll
2013	\$ 480,700,326	\$ 299,657,530	\$ 181,042,796	\$ 2,706,170,349	11.07%
2014	\$ 479,884,486	\$ 362,462,537	\$ 117,421,949	\$ 2,718,100,677	1334%

Notes to Schedule

Methods and Assumptions Used to Determine Contribution Rates

Actuarial Cost Method	Entry Age Normal
Amortization Method	Level Percentage of Payroll
Remaining Amortization Period	Amortized over a closed thirty year period from June 30, 2012 ending June 30, 2042
Asset Valuation Method	Five year smoothed market
Inflation	3.00%
Salary Increases	Composed of 3.00% inflation, plus 1.25% productivity increase rate, plus step rate promotional increases for members with less than ten years of service.
Investment Rate of Return	7.75%
Retirement Age	Experience based table of rates based on age and service. Adopted by ERB on April 26, 2013 in conjunction with the six year experience study for the period ending June 30,
Mortality	90% of RP-2000 Combined Mortality Table with White Collar Adjustment, projected to 2014 using Scale AA (with one year setback for females).

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF REVENUES AND EXPENSES
BUDGET AND ACTUAL
For the Year Ended June 30, 2014

	Original Budget	Final Budget	Actual Budgetary Basis	Variance - Final Budget Favorable (Unfavorable)
Revenues:				
Other State Funds	\$ 31,971,300	31,971,300	31,971,300	-
Total budgeted revenue	<u>\$ 31,971,300</u>	<u>31,971,300</u>	<u>31,971,300</u>	<u>-</u>
Expenses:				
Personal services and employee benefits	\$ 5,758,400	5,758,400	5,104,000	654,400
Contractual services	25,387,400	25,387,400	24,221,400	1,166,000
Other Costs	825,500	825,500	742,600	82,900
Total expenses	<u>\$ 31,971,300</u>	<u>31,971,300</u>	<u>30,068,000</u>	<u>1,903,300</u>
Reconciliation of GAAP basis to budgetary basis:				
Revenue GAAP Basis			\$ 2,078,209,458	
Net appreciation (depreciation) in investment value			1,587,002,625	
Investment advisor and custody fees			(13,719,779)	
Current year revenue not needed for budgeted expenses			(3,619,521,004)	
Revenue - budgetary basis			<u>\$ 31,971,300</u>	
Expenses GAAP basis - administrative			\$ 16,516,696	
Depreciation expense			(168,475)	
Investment advisor and custody fees			13,719,779	
Expenses - budgetary basis			<u>\$ 30,068,000</u>	

**STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF CASH ACCOUNTS
As of June 30, 2014 and 2013
(Unaudited)**

**Educational Employees' Retirement Fund
Pension Trust Account
Fund 60500**

	2014	2013
Petty cash	\$ 100	\$ 100
Qualified Excess Benefit Arrangement Trust	211,210	23,836
Checking Account at Wells Fargo Bank	1,804,456	5,353,975
Short-term investment accounts:		
Overnight repurchase agreement pool - State Treasurer		
Short Term Investment Funds - STIF	<u>275,693,396</u>	<u>746,599,116</u>
Balance per financial statements	<u>\$ 277,709,162</u>	<u>\$ 751,977,027</u>
Pledged collateral for Wells Fargo demand deposit account:		
Total amount on deposit at June 30	\$ 211,210	\$ 23,836
Less Federal Deposit Insurance Corporation coverage	<u>(211,210)</u>	<u>(23,836)</u>
Total uninsured public funds	<u>\$ -</u>	<u>\$ -</u>

**STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF ADMINISTRATIVE, CONSULTANT, AND
BUDGETED INVESTMENT EXPENSES
For the Year Ended June 30, 2014**

	<u>2014</u>
Personal Services and Benefits	
Salaries	\$ 3,253,235
Benefits	1,850,442
Total Personal Services and Benefits	<u>5,103,677</u>
Consultant Services	
Medical Review Board Fees	\$ 19,993
Audit Fees	85,566
Legal Fees	2,290,289
Information Technology Fees	1,695,229
Other Consultant Services Fees	6,526,900
Total Consultant Services Expenses	<u>10,617,977</u>
Budgeted Investment Expenses	
Custodial Expenses	\$ 392,955
Investment Manager Expenses	
Domestic Fixed Income	5,149,426
Domestic Equity	2,237,924
Non-US Equity	2,909,801
Non-US Fixed Income	410,413
Investment Consulting Expenses	1,614,677
Other Investment Expenses	1,004,583
Total Budgeted Investment Expenses	<u>\$ 13,719,779</u>
Other Administrative Expenses	
Building and Maintenance	\$ 150,382
Dues and Subscriptions	37,430
Employee and Board Travel	64,748
Inventory and Supplies	54,244
IT Equipment	151,158
Training and Education	12,952
Telecommunication Services	100,807
Utilities	31,085
Other Miscellaneous Expenditures	118,739
Total Other Administrative Expenses	<u>721,544</u>
Total Administrative, Consultant & Budgeted Investment Expenses	<u>\$ 30,162,978</u>

**STATE OF NEW MEXICO
EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF ACCOUNTABILITY IN GOVERNMENT ACT
PERFORMANCE MEASURES
As of June 30, 2014
(Unaudited)**

Type	Description	Target	Actual
Outcome	Average number of days to process refund requests	15	8
Outcome	Percentage of member satisfaction with seminars and trainings	95%	98%
Outcome	Average rate of return over a cumulative five-year period	7.75 %	12.90 %
Output	Number of benefit estimates and purchase of service requests computed annually	7,000	6,725
Output	Number of member workshops conducted	30	28
Outcome	Funding period of UAAL in years	≤ 30	42.1

**REPORT OF INDEPENDENT AUDITORS ON INTERNAL CONTROL OVER FINANCIAL
REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

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

We have audited, in accordance with the 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, the Statements of Fiduciary Net Position and Statements of Changes in Fiduciary Net Position of the New Mexico Educational Retirement Board (the "ERB") as of and for the years ended June 30, 2014 and 2013, and the related notes to the financial statements, which collectively comprise the ERB's basic financial statements, and the Schedule of Revenues and Expenses-Budget to Actual presented as supplementary information, as defined by the Government Accounting Standards Board, as of and for the year ended June 30, 2014, and have issued our report thereon dated December 15, 2014.

Internal Control Over Financial Reporting

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

A *deficiency in internal control* 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 and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses.

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

However, material weaknesses may exist that have not been identified. We did identify a deficiency in internal control, described in the Schedule of Findings and Responses as item 2014-002 to be a significant deficiency in internal control over financial reporting.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether ERB's financial statements are free from 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 instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and responses as items 2014-001.

ERB's Response to Findings

ERB's response to the findings identified in our audit are described in the accompanying schedule of findings and responses. ERB's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Mess Adams LLP

Albuquerque, New Mexico
December 15, 2014

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF STATUS OF PRIOR YEAR AUDIT FINDINGS
For the Year Ended June 30, 2014

2013-001	Timely Deposits – Non-compliance	Resolved
2013-002	Financial Close & Reporting Untimely Reconciliations – Non-compliance	Resolved

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF FINDINGS AND RESPONSES
For the Year Ended June 30, 2014**

A. OTHER MATTERS AS REQUIRED BY THE NEW MEXICO STATE AUDIT RULE

2014-001 Regulations Governing the Per Diem and Mileage Act– Non-compliance

CONDITION

In 1 out of 8 transactions tested, we noted that mileage expense was reimbursed at the incorrect rate.

CRITERIA

In accordance with Section 10-8-1 to 10-8-8 NMSA 1978 2.42.2 NMAC governs the payment of per diem rates and mileage and the reimbursement of expenses for all salaried and non-salaried public officers and employees of the state agencies. Public officers and employees of state agencies shall be reimbursed for mileage accrued in the use of a private automobile in the discharge of official duties as follows:

“Unless the secretary has reduced the rates set for mileage for any class of public officials and for employees of state agencies pursuant to Section 10-8-5 (D) NMSA 1978, 80% of the internal revenue service standard mileage rate set January 1 of the previous year for each mile traveled in a privately owned vehicle.”

The effective rate for the transaction tested was \$0.44 per mile as of October 21, 2013.

EFFECT

Auto travel of 19.2 miles was reimbursed at a rate of \$2 per mile, instead of the \$.44 per mile resulting in an overpayment of \$29.95. Consequently, the Agency was not in compliance with 2.42.2 NMAC.

CAUSE

The Agency has well designed controls regarding the review of all travel and mileage related expenses. However, the forms reviewed are hard copies making it necessary to manually recalculate the expense detail. The controls were not fully implemented as there was a miscalculation within the expense detail that was not detected during review.

RECOMMENDATION

Attention should be made to reviewing the calculation that comprises the total reimbursement. Reimbursement requests not properly reviewed and approved in accordance with statute and regulation significantly increase the risk of fraudulent payment requests.

MANAGEMENT RESPONSE

Management concurs that an error occurred on the identified travel voucher and that a more comprehensive review of the document would have identified the problem, ERB has added this review step, identified and implemented additional required information on the forms we use, strengthened reviewer cross training, and verified that our procedural documentation is in place and current. The reimbursement overage of \$29.95 was promptly recouped from the employee involved.

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF FINDINGS AND RESPONSES
For the Year Ended June 30, 2014**

A. OTHER MATTERS AS REQUIRED BY THE NEW MEXICO STATE AUDIT RULE

2014-002 Financial Close and Reporting of the Investment Cycle (Significant Deficiency)

CONDITION

The financial close and reporting process is important to achieving reliable financial reporting. Weaknesses in this process can elevate the risks of misstatement in the financial statements. In obtaining our understanding of management's procedures with regard to the financial close and reporting process, generally we consider processes and controls for the following areas:

- Communication of the financial close and reporting process among the appropriate departments and individuals.
- Authorization for significant transactions outside the normal course of business.
- Evaluation of significant accounting estimates.
- Timely preparation of the trial balance and closing reconciliations.
- Procedures for summarizing general ledger data.
- Review and approval of the financial statements and disclosures.

CRITERIA

The financial close and reporting process over the investment cycle should provide management with clear processes that provides a transparent audit trail from the custody bank statements to the general ledger.

CAUSE

Investment activity is reviewed and reconciled consistently by the Investment Department throughout the year. The Accounting Department has an established control process which relies on reviewing the monthly reconciliation summaries and analyzing the activity to adjust the general ledger accounts accordingly at year end. This process requires communication between the departments and timely completion to ensure the general ledger accounts are reflected properly for financial statement preparation.

There was a lack of communication among the Departments during financial close and reporting this fiscal year. Some unique transactions occurred that the Investment Department was aware of and accounting for within their schedules; however that information apparently was not clearly communicated to the Accounting Department. For example, some funds were mistakenly remitted to State Street custody bank prior to June 30, 2014. The funds were returned and remitted to JP Morgan; however, they were received after June 30, 2014 and rejected by JP Morgan. Consequently, this activity was not recorded on the JP Morgan statements. The Accounting Department proceeded with adjusting general ledger activity to agree with the statements, and was unaware of this additional reconciling item.

STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
SCHEDULE OF FINDINGS AND RESPONSES
For the Year Ended June 30, 2014

A. OTHER MATTERS AS REQUIRED BY THE NEW MEXICO STATE AUDIT RULE

2014-002 Financial Close and Reporting of the Investment Cycle (Significant Deficiency)
(Continued)

Further, turnover occurred in the CFO position. The processes for capturing and reconciling the monthly activity did not change; however, this was not consistent with general ledger reporting. The reconciliations performed on a monthly basis were done correctly, and should have been accumulated to record final balances.

EFFECT

There is potential for accounting errors going undetected and inaccurate financial reporting.

RECOMMENDATION

We believe that it is critical for Management to establish a control process regarding the reconciliation and recording of investment balances as the Agency transitions to a new custody bank, State Street. We also recommend that the designed process includes monthly posting to the general ledger by the Accounting Department rather than recording investment activity at the end of the fiscal period.

The Accounting and Investment departments need to improve communication during the financial close and reporting process to ensure the provided trial balance ready for audit reflect final balances and can be supported by reconciliations and custody bank statements.

MANAGEMENT RESPONSE

Management concurs that a timely financial close and reporting process is important to managing ERB's investments. In addition, management recognizes that interdepartmental communication is critical to successful information management. Several concurrent business activities impacted the timing of this year's year end close: software system upgrade testing, critical interagency reporting projects mandated by the Department of Finance and Administration, transition to a new investment custody bank, and personnel changes. In the midst of these changes we were not as responsive to closing requirements as in prior years. ERB Accounting has revised its monthly investment statement reconciliation and posting process which will enable the accounting and investment workgroups to confirm and agree the results of their separate processes throughout the year to improve financial reporting.

**STATE OF NEW MEXICO EDUCATIONAL RETIREMENT BOARD
EXIT CONFERENCE
Year Ended June 30, 2014**

Board staff prepared the Management's Discussion & Analysis ("MD&A"), financial statements, statements, schedules, and notes for the fiscal years ended June 30, 2014 and 2013. 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 12, 2014. The following individuals attended this exit conference:

Educational Retirement Board

Members of the Audit Committee –
Mary Lou Cameron, Audit Committee Chairperson
H. Russell Goff, Vice-Chairman

Agency Management –
Jan Goodwin, Executive Director
Rick Scroggins, Deputy Director
Dianne L. Rossbach, Chief Financial Officer

Moss Adams LLP

Jeff Bridgens, Senior Manager

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