

**STATE OF NEW MEXICO PUBLIC EMPLOYEES'  
DEFERRED COMPENSATION PLAN  
Santa Fe, New Mexico**

**FINANCIAL STATEMENTS  
June 30, 2018 and 2017**

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## Independent Auditor's Report

To the State Auditor, Board of Directors, and PERA  
The State of New Mexico Public Employees'  
Deferred Compensation Plan  
Santa Fe, New Mexico

### Report on the Financial Statements

We have audited the accompanying statements of net position held in trust for plan benefits of the State of New Mexico Public Employees' Deferred Compensation Plan (the Plan) as of June 30, 2018 and 2017 and the related statements of changes in net position held in trust for plan benefits for the years then ended, and the related notes to the financial statements, which collectively comprise the basic financial statements as listed in the accompanying 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.

### Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller 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 entity'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.

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

## **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Plan as of June 30, 2018 and 2017, and the results of its operations for the years then ended 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 on pages 3 through 8, 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 assurance.

### *Other Information*

Our audit was conducted for the purpose of forming an opinion on the basis financial statements that collectively comprise the Plan's financial statements. The Memorandums of Understanding, Officials Roster and Exit Conference are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such additional information has not been subject to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

### **Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated October 25, 2018 on our consideration of the Plan'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 solely to describe the scope of our testing of internal controls over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Plan's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.

A handwritten signature in black ink that reads "Eide Bailly LLP". The signature is written in a cursive, flowing style.

Boise, Idaho  
October 25, 2018

**STATE OF NEW MEXICO PUBLIC EMPLOYEES’  
DEFERRED COMPENSATION PLAN  
MANAGEMENT’S DISCUSSION AND ANALYSIS  
JUNE 30, 2018 AND 2017**

This discussion and analysis of the State of New Mexico Deferred Compensation Plan’s (“the Plan”) financial performance provides an overview of the Plan’s financial activities for the fiscal years ended June 30, 2018, 2017 and 2016. This section should be read in conjunction with the Plan’s financial statements.

**Using This Annual Financial Report**

This annual financial report consists of two parts: (1) management’s discussion and analysis (this section) and (2) the Plan’s basic financial statements. The financial statements also include notes that explain information in the financial statements and provide more detailed data.

**Condensed Financial Information**

The table below compares key financial information in a condensed format between the current and prior years:

	Fiscal Years Ended June 30		
	2018	2017	2016
<b>Plan Net Position Held in Trust for Plan Participants</b>	\$ 606,862,949	\$ 568,832,783	\$ 502,840,009
Employee Contributions	\$ 40,031,630	\$ 47,752,984	\$ 35,261,360
Net change in fair value of investments	44,425,527	56,218,055	(1,020,238)
Interest Income	3,054,074	2,739,314	2,516,513
Benefits Paid	(48,221,377)	(39,510,967)	(34,153,732)
Administrative Expenses	(1,225,808)	(1,164,518)	(1,055,123)
Life Insurance Premiums	(33,880)	(42,094)	(55,038)
<b>Net Increase in Plan Net Position</b>	\$ 38,030,166	\$ 65,992,774	\$ 1,493,742

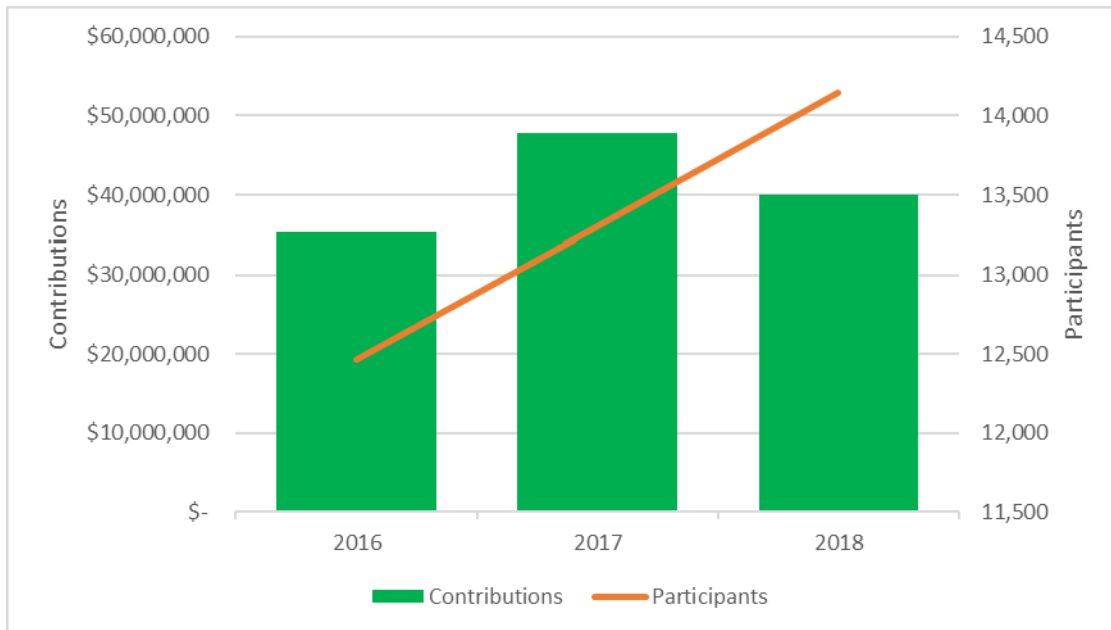
**Financial Highlights**

The net position held in trust for plan benefits increased by approximately \$38 million during the current period from \$568.8 million at June 30, 2017 to \$606.8 million at June 30, 2018. This increase is primarily due to investment income earned during the current year interest income from the Stable Value Option, as well as an increase in participants. The net position held in trust for plan benefits increased by approximately \$66 million from \$502.8 million at June 30, 2016 to \$568.8 million at June 30, 2017. This increase was primarily due to the Bernalillo County conversion from ICMA and Valic to PERA SmartSave.

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*Contributions to the Plan*

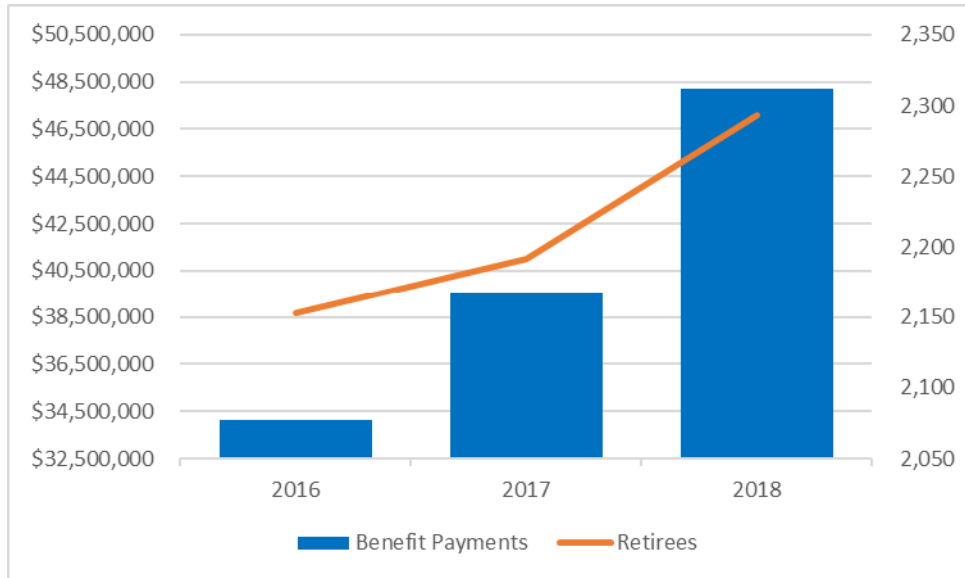
Employee contributions were \$40.0, \$47.8 and \$35.2 million for the years ending June 30, 2018, 2017 and 2016, respectively. Employee contributions decreased by \$7.7 million from June 30, 2017 to June 30, 2018 and increased by \$12.5 million from June 30, 2016 to June 30, 2017. Fluctuations in employee contributions are primarily due to differences in the number of actively contributing participants from year to year as well as changes in the average contributions per participant. The average contribution per participant was \$2,828, \$3,590, and \$2,829 for the year ended June 30, 2018, 2017 and 2016, respectively. There were 14,144, 13,300, 12,462 actively contributing participants at June 30, 2018, 2017 and 2016, respectively. In accordance with the Internal Revenue Code, employees could voluntarily contribute up to a maximum amount of \$18,000 in 2017 and \$18,500 in 2018 unless over age 50, which allows an additional \$6,000. However, participants' contributions are not always at maximum, causing uneven annual contribution changes in relation to participant changes.



*Beneficiaries of the Plan*

Benefits paid to participants increased from \$39.5 million for the year ended June 30, 2017 to \$48.2 million for year ended June 30, 2018. This was due to an increase in assets being requested along with an increase to the number of retirees from 2,153 in 2017 to 2,293 in 2018. During the previous period, benefits paid to participants increased from \$34.2 million for the year ended June 30, 2016 to \$39.5 million for year ended June 30, 2017. There was a minimal change in the number of retirees, from 2,192 in 2016 to 2,153 in 2017, but an increase in average distribution. The average distribution per participant was \$21,020, \$18,369, and \$15,617 for the years ended 2018, 2017 and 2016, respectively. The number of participants who withdraw funds from the plan due to termination of employment on an annual basis fluctuates. The number of participants who withdraw funds has risen from 1,130 in 2016 to 1,305 in 2017 to 1,459 in 2018.

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**Overall Fund Structure and Objectives**

The Plan was established in accordance with the provisions of the State of New Mexico Deferred Compensation Act, NMSA 1978, Section 10-7A-1 through 10-7A-12 (2017). The Plan complies with the requirements of Internal Revenue Code Section 457, as amended. The Plan provides a voluntary, supplemental tax-deferred retirement program, which provides employees a convenient means to save for retirement. The Public Employees Retirement Association (“PERA”) of New Mexico is the Trustee of the Plan. PERA is directed by the Public Employees Retirement Board (the “Board”) which consists of twelve members.

After an employer has adopted the Plan and the PERA Board has approved the adoption, an employee is eligible to participate in the Plan as of the first day of employment and may voluntarily contribute a portion of their compensation up to the annually established Internal Revenue Service limits. Under Plan provisions, employees of the State, its cities and counties, special districts and educational institutions are eligible to contribute to the Plan through payroll deductions. An employee participating in the Plan may discontinue, or temporarily suspend, contributions at any time. Employees can increase or decrease contribution amounts at any time. If the participant elects to contribute, the minimum amount that may be contributed for any Plan year is \$260 and shall not exceed the amount permitted pursuant to Section 457 of the Internal Revenue Code.

**Costs of the Plan**

The Plan seeks to maintain low costs for employees that elect to participate. In 2017-2018, the cost of providing recordkeeping, enrollment, education, and other administrative services to participants in the Plan was \$7.50 plus .135% of assets, not to exceed \$26 per quarter, per participant. Investment consulting services were provided at an average cost of \$1.02 per quarter, per participant. PERA operating fees averaged \$1.00 per quarter, per participant. Additional fees and other charges may be

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assessed for various options available in the Plan. In addition, the Plan seeks to provide the best possible investment vehicles at the lowest cost.

**Asset Allocation**

With the investment choices as are made available and those policies or procedures as are determined by the Board and the administration from time to time. The Plan has no control over investment decisions made by the participants. Plan assets may be invested and reinvested in various instruments as deemed appropriate by the Board and Plan management. Several investment tiers have been developed and made available to participants. A summary of the types of investments is listed in Note 3 in the notes to the financial statements.

**Market Environment Overview**

The fiscal year was largely a story of two environments. In 2017, we saw synchronized global growth, low volatility, tax cuts in the U.S. at year-end, and a weak U.S. dollar. During the last two quarters of 2017 most asset classes were up, particularly riskier ones. Emerging markets lead the way in Q3 (+7.9%<sup>1</sup>) and Q4 (+7.4%<sup>1</sup>). U.S. and international equities also posted strong returns over both quarters, while fixed income assets were largely up but with more modest returns in the risk on environment.

The trends of 2017 persisted into early 2018, but the environment quickly changed. In 2018, we have seen volatility increase from its very low levels, interest rates and inflation rise, the U.S. dollar rebound, and trade tensions between the U.S. and others heat-up. In this environment, U.S. equities were one of the few asset classes to perform, while international equities and most fixed income asset classes fell. High yield bonds did post a modest gain (+0.2%<sup>2</sup>) in the first two quarters of 2018.

The net result of the two environments on the fiscal year returns ending June 2018 was that equities increased, particularly in the U.S, while in fixed income TIPS and high yield bonds posted relatively modest returns and the broad U.S. bond market slightly declined. Emerging market bonds fell.

For the fiscal year, U.S. equities, as represented by the Russell 3000, rose +14.8%. The trend of U.S. growth stocks outperforming value stocks persisted and small capitalization stocks (+17.6%) outperformed large capitalization (+14.5%) and mid-capitalization (+12.3%) stocks. The MSCI EAFE, representing foreign developed markets, increased at less than half the rate of U.S. equities, up +6.8%. Emerging market equities’ strong returns in 2017 were balanced by an 8.0% decline in the second quarter of 2018 as a stronger dollar and trade tensions weighed on results. The MSCI Emerging Markets Equity index gained +8.2% for the full fiscal year.

Within fixed income, positive returns in the final two quarters of 2017 moved to concerns over rising interest rates and inflation creating headwinds in 2018. In the U.S., the Federal Reserve increased interest rates for the seventh time in June to a range of 1.75% to 2.00% and continued to reduce its balance sheet. The rate increases contributed to the flattening of the U.S. yield curve during the fiscal year. Over the trailing year, TIPS (+2.1%) and high yield bonds 2 (+2.6%) increased, while the broad U.S. bond market, represented by the Barclays Aggregate Index, fell 0.4%. Similar to emerging market equities, returns for emerging market bonds in the second quarter of 2018 weighed on the fiscal year results. In this case, more dramatically as the 10.4% decline in the second quarter for emerging market bonds (as represented by JPM GBI-EM Global Diversified – Local Currency) led to a -2.3% return for the trailing year.



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Within other asset classes, natural resource stocks (S&P Global Natural Resources Index) rose +24.8%, commodities (Bloomberg Commodity Index) gained +7.4%, and REITS (MSCI U.S. REIT Index) gained +3.6%. Oil prices finished the fiscal year at over \$60/barrel, representing a dramatic increase from their recent lows. Cuts from OPEC and strong growth globally contributed to the rise in oil prices.

Looking forward, there are several issues that we continue to monitor. First, is the potential for major central banks to tighten monetary policy at the same time. Second, in the U.S., equity markets remain extended and the latest economic cycle has been long. Also in the U.S., trade policy remains another key issue. Next, is the declining growth in China and the impact of trade tensions with the U.S. Finally, political uncertainty and ongoing structural issues remain a concern in Europe.

After an extended period of monetary support through low interest rates and bond purchases from banks (i.e., quantitative easing), we could be moving into a period where central banks pull back support at the same time. The U.S. is further along in that process with the Federal Reserve increasing interest rates and reducing its balance sheet. It is also largely expected that the European Central Bank (ECB) will end its quantitative easing by year-end. If central banks begin pulling back support this could put further upward pressure on rates, weigh on economic growth, and tighten liquidity.

The U.S. economy and equity markets have experienced a long period of growth since the Global Financial Crisis due in part to central bank support. Late cycle dynamics of low unemployment and rising inflation are in place and valuations are stretched for equities. It is inevitable that growth will eventually slow and equity markets pull back, but the question is when. Other key issues in the U.S. include policy uncertainty related to tariffs, immigration, and strategic alliances.

China has the second largest economy behind the U.S. After a long period of growth through government investment, it continues to manage a repositioning of its economy to one of consumption. This has led to a slowing of its economy and has hurt countries that depend on its trade. The recent trade tariffs between the U.S. and China is another key issue, which could have a disproportionately negative impact on China, as the U.S. is one of their largest export destinations. Another key issue in China remains the high debt levels, particularly in the corporate sector.

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Europe continues to have the structural issue of having a single currency and central bank with fiscal policy resting with each individual country. Consequently, countries that are experiencing financial difficulties are unable to use the traditional tools of lowering interest rates and devaluing their currency to stimulate growth. This has caused tensions within the Eurozone as highlighted by the recent elections in Italy and the prior elections in Germany, as well as the on-going issues in Greece. Given the size of Italy’s bond market and economy within the euro area a sovereign debt crisis or departure from the euro would have significant consequences. The Plan’s investment consultant will continue to monitor these issues and others.

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<sup>1</sup> MSCI Emerging Markets Index

<sup>2</sup> Barclays High Yield

### **Contacting Management**

This report is designed to provide the Board, Plan participants, investors and creditors with a general overview of the Plan’s finances and to demonstrate the Plan’s accountability for the Plan’s funds. For additional information, contact the NM PERA Deferred Compensation Plan Manager at 33 Plaza La Prensa, Santa Fe, New Mexico 87507 or 1-800-342-3422.

## **BASIC FINANCIAL STATEMENTS**

**STATE OF NEW MEXICO PUBLIC EMPLOYEES'  
DEFERRED COMPENSATION PLAN  
STATEMENTS OF NET POSITION HELD IN TRUST FOR PLAN BENEFITS  
June 30, 2018 and 2017**

	<u>2018</u>	<u>2017</u>
<b>INVESTMENTS</b>		
Annuities	\$ 1,062,992	\$ 1,197,477
Stable value option	129,567,328	131,884,328
Variable earnings investments	457,990,195	418,943,401
Self-directed option	<u>4,954,319</u>	<u>4,629,288</u>
 Total investments	 593,574,834	 556,654,494
<b>RECEIVABLES</b>		
Participant contributions receivable	993,246	860,212
Participant loans receivable	<u>12,294,869</u>	<u>11,318,077</u>
 <b>NET POSITION HELD IN TRUST FOR PLAN BENEFITS</b>	 <u><u>\$ 606,862,949</u></u>	 <u><u>\$ 568,832,783</u></u>

The accompanying notes are an integral part of the financial statements.

**STATE OF NEW MEXICO PUBLIC EMPLOYEES'  
DEFERRED COMPENSATION PLAN  
STATEMENTS OF CHANGES IN NET POSITION HELD IN TRUST FOR PLAN BENEFITS  
Years Ended June 30, 2018 and 2017**

	<u>2018</u>	<u>2017</u>
<b>ADDITIONS TO NET POSITION ATTRIBUTED TO</b>		
Employee contributions	\$ 40,031,630	\$ 47,752,984
Investment income:		
Net increase in fair value of investments	44,425,527	56,218,055
Interest income on stable value option	2,495,178	2,259,191
Interest income on fixed annuity payout	19,467	19,467
Interest income on participant loans	539,429	460,656
	<u>87,511,231</u>	<u>106,710,353</u>
<b>DEDUCTIONS FROM NET POSITION ATTRIBUTED TO</b>		
Benefits paid to participants	48,221,377	39,510,967
Administrative expenses	1,225,808	1,164,518
Life insurance premiums	33,880	42,094
	<u>49,481,065</u>	<u>40,717,579</u>
<b>NET INCREASE</b>	38,030,166	65,992,774
<b>NET POSITION HELD IN TRUST FOR PLAN BENEFITS, BEGINNING OF YEAR</b>	<u>568,832,783</u>	<u>502,840,009</u>
<b>NET POSITION HELD IN TRUST FOR PLAN BENEFITS, END OF YEAR</b>	<u>\$ 606,862,949</u>	<u>\$ 568,832,783</u>

The accompanying notes are an integral part of the financial statements.

**STATE OF NEW MEXICO PUBLIC EMPLOYEES'  
DEFERRED COMPENSATION PLAN  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2018 and 2017**

**NOTE 1 – DESCRIPTION OF PLAN**

**General**

The State of New Mexico (the State) Public Employees' Deferred Compensation Plan (the Plan), a defined contribution plan, was established pursuant to the Deferred Compensation Act of New Mexico, which was passed on April 6, 1981. The Plan was approved by the State Department of Finance and Administration on January 6, 1982, and is sponsored by the State. The Plan is administered by the New Mexico Public Employees' Retirement Association (NMPERA).

**Contributions**

Under Plan provisions, employees of the State, its cities and counties, special districts and educational institutions that have completed the Plan adoption process, are eligible to contribute into the Plan through payroll deductions. There were approximately 81,500 and 80,000 employees eligible to participate in the Plan as of June 30, 2018 and 2017, respectively. In accordance with Section 457 of the Internal Revenue Code (IRC), the Plan limits the amount of an individual's annual contribution to 100% of annual gross includable compensation, not to exceed \$18,500 for calendar years 2018 and \$18,000 for calendar year 2017. Additionally, in each of the three Retirement Catch-up years, a participant's Retirement Catch-up contribution is limited to the lesser of (a) the maximum amount for that year, \$18,500 in 2018 and \$18,000 in 2017 or (b) the amount by which contributions to the Plan in previous years were less than the maximum that the participant was eligible to contribute. An additional \$6,000 in 2018 and in 2017 can apply to a participant reaching the age 50 and each year thereafter. This catch-up provision is referred to as the Age 50 and Over Catch-up contribution. Amounts contributed by employees are deferred for federal and state income tax purposes until benefits are paid to the employees. Participant employers do not make any contributions to the Plan.

Under provisions of the Small Business Job Protection Act of 1996 (SBJPA), which became effective for Plan years beginning after December 31, 1996, assets of the IRC Section 457 Plan must be held in a trust, custodial account, or annuity contract, for the exclusive benefit of employees and beneficiaries and will no longer be solely the property of the employer and subject only to claims of the employer's general creditors. At June 30, 2018 and 2017, the Plan met the requirements of the SBJPA.

Although this is no longer offered as an option for new participants, at retirement or termination of employment, employees already investing in universal life insurance contracts may continue to make premium payments directly to the insurance carrier or they may receive the cash surrender value of the policies. In the case of the death of an employee, the face value of the insurance contract is payable to the policy beneficiary.

**Investment Options**

Employees electing to participate in the Plan may contribute to any of the following options:

- Variable earnings investments consisting of various publicly-traded mutual funds;
- Stable value option managed by Galliard Capital Management; and
- Self-directed brokerage account option administered by Charles Schwab.

**STATE OF NEW MEXICO PUBLIC EMPLOYEES’  
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**NOTE 1 – DESCRIPTION OF PLAN (CONTINUED)**

**Participant Loans**

The Plan allows participants to take loans from their account balances. Any participant is eligible to receive a loan. Each participant is entitled to one outstanding loan at a time. Participants are charged a nonrefundable loan set-up fee of \$50. An additional annual fee of \$50 is assessed on the anniversary date of the loan while the loan is outstanding. Repayments of loans are to be made automatically from a participant-specified account with a financial institution. The maximum term permitted on a loan is five years or 15 years if the loan is for the purchase of a principal residence. The minimum loan amount permitted is \$1,000 and the maximum amount of any loan under the Plan is the lesser of 50% of the participant’s vested account balance or \$50,000. The total balance of loans outstanding to participants was \$12,294,869 and \$11,318,077 at June 30, 2018 and 2017, respectively and is listed as participant loans receivable on the Statement of Net Position Held in Trust for Plan Benefits. Interest rates range between 3.75% and 9.25% need to verify for all loans outstanding. The interest rate is based on market conditions at the time the loan is processed. Generally, the rate is the “Prime Rate” + 1%.

**Payment of Benefits**

A Plan distribution can become available only after the participant reaches the age of 70½ years old, the participant’s death, separation-from-service, retirement, upon the participant’s severe financial emergency, or if a participant’s account balance does not exceed \$5,000 and no amount was deferred during a 2-year period and there was no prior distribution. Participants may select various payout options, including lump sum payments or payments over various periods.

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Significant accounting policies followed by the Plan are as follows:

**Basis of Accounting**

The accompanying financial statements have been prepared on the accrual basis of accounting.

**Use of Estimates in Preparing Financial Statements**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America may require management to make estimates and assumptions that affect amounts reported in financial statements and accompanying notes. Actual results may differ from those estimates.

**Prior Year Reclassification**

Certain prior year amounts have been reclassified for consistency with the current year presentation. These reclassifications had no effect on the reported results of operations. Interest income for the Stable Value Option has been separately presented in the Statement of Changes in Net Position Held in Trust for Plan Benefits.

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NOTES TO FINANCIAL STATEMENTS  
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**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Investment Valuation and Income Recognition**

Investments in the fixed annuity payout option are valued based upon the fixed earnings rates as reported by the investment carriers or manager, which approximate fair value. Investments in the Stable Value Option are valued based upon the daily net asset value reported daily by Galliard Capital Management, which approximates fair value. The investment valuation includes contributions received, plus investment income earned to date less applicable charges and amounts withdrawn.

Variable earnings investments in publicly-traded mutual funds are presented at fair value based upon published quotations. All purchases and sales of investments are recorded on a trade-date basis.

Assets held in fixed and variable annuity payout investments represent discontinued annuity payout options in the Plan. The Plan held \$1,062,992 and \$1,197,477 at June 30, 2018 and 2017, respectively, which represents assets transferred to a product provider for investment in fixed and variable group annuity contracts. Periodic payments are made to retired participants of the Plan as provided by these purchased annuity contracts. The contract valuation of these assets is based upon an actuarial valuation of the present value of future retirement benefits to be paid under the contracts, which approximates fair value. Annuity payout investments are no longer available as options in the Plan.

**Contributions and Contributions Receivable**

Contributions are recognized when amounts are withheld from employees. Contributions receivable represents amounts withheld from employees, but not remitted to the investment carriers at June 30, 2018 and 2017. The Plan requires that contributions received “in good order” by the Plan Administrator from the various Plan payroll centers be applied to the respective participant account within one business day following the date of receipt.

**Interest Income**

Interest income for the fixed annuity payout option and participant loans is recorded as earned on the accrual basis.

The annual crediting interest rate for the stable value investment option, net of fees, ranged from 1.74% to 1.92% for the year ended June 30, 2018, and 1.65 % to 1.78% for the year ended June 30, 2017. Interest income for the stable value investment option is recorded as earned on the accrual basis.

**Variable Earnings Investment Income**

Variable earnings investment income consists of dividends earned and realized and unrealized gains and losses attributed to the mutual funds supporting the variable earnings investments. Dividends are recorded on the ex-dividend date.



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**NOTE 3 – INVESTMENTS AND DEPOSITS**

The State of New Mexico Public Employees' Deferred Compensation Plan categorizes the fair value measurements of its investments based on the hierarchy established by generally accepted accounting principles. The fair value hierarchy, which has three levels, is based on the valuation inputs used to measure an asset's fair value: Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs.

Investments, including derivative instruments that are not hedging derivatives, are measured at fair value on a recurring basis. Recurring fair value measurements are those that Governmental Accounting Standards Board (GASB) Statements require or permit in the statement of net position at the end of each reporting period.

Mutual Funds: Valued at the daily closing price as reported by the fund. Mutual funds held by the Plan are open-ended mutual funds that are registered with the Securities and Exchange Commission. These funds are required to publish their daily net asset value (NAV) and to transact at that price. The mutual funds held by the plan are deemed to be actively traded.

Self-directed investments: Valued at the daily closing price as reported by the fund and reported as Level 1. These represent investments that are actively traded on an open market.

Lifecycle funds: Valued at carrying value based on the NAV of the observable market prices of the underlying assets within that account less liabilities.

	June 30, 2018	Fair Value Measurements Using:		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investments at Fair Value:				
Mutual Funds	\$ 304,582,371	\$ 304,582,371	\$ -	\$ -
Self-directed investments	4,954,319	4,954,319	-	-
Total Investments at Fair Value	309,536,690	\$ 309,536,690	\$ -	\$ -
Investments at Net Asset Value:				
Lifecycle Funds	153,377,900			
Investments at Contract Value:				
Stable value option	129,567,328			
Annuities, net of payments in transit	1,092,916			
Total Investments	\$ 593,574,834			

**STATE OF NEW MEXICO PUBLIC EMPLOYEES'  
DEFERRED COMPENSATION PLAN  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2018 and 2017**

**NOTE 3 – INVESTMENTS AND DEPOSITS (CONTINUED)**

	Fair Value Measurements Using:			
	June 30, 2017	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investments at Fair Value:				
Mutual Funds	\$ 282,812,855	\$ 282,812,855	\$ -	\$ -
Self-directed investments	4,629,288	4,629,288	-	-
Total Investments at Fair Value	<u>287,442,143</u>	<u>\$ 287,442,143</u>	<u>\$ -</u>	<u>\$ -</u>
Investments at Net Asset Value:				
Lifecycle Funds	136,211,881			
Investments at Contract Value:				
Stable value option	131,884,328			
Annuities, net of payments in transit	<u>1,116,142</u>			
Total Investments	<u><u>\$ 556,654,494</u></u>			

Investments measured at the net asset value (NAV):	Fair Value	Unfunded Commitments	Redemption Frequency	Redemption Notice
June 30, 2018				
Lifecycle Funds	\$ 153,377,900	\$ -	Daily	None
June 30, 2017				
Lifecycle Funds	\$ 136,211,881	\$ -	Daily	None

Lifecycle Funds: This asset class is generally comprised of a combination of fixed income and equity investment options. These investment options may include balanced, asset allocation, target-date, and target-risk investment options. Although typically lower risk than investment options that invest solely in equities, all investment options in this category have the potential to lose value.

Stable value option and annuities: The plan invests in annuities that represent guaranteed investment contracts that represent a fixed-income security portfolio of fixed-income securities and a value guarantee (wrapper) provided by a third party and are reported at contract value. Contract value represents contributions made under the contract, plus earnings, less participant withdrawals and administrative expenses. Under the contract, a crediting interest rate is established that provides a minimum guaranteed annual interest rate. Participant initiated transactions are at contract value. However, certain events initiated at the Plan level, specifically termination of the contract, might limit the ability to the plan to transact at contract value.

**STATE OF NEW MEXICO PUBLIC EMPLOYEES’  
DEFERRED COMPENSATION PLAN  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2018 and 2017**

**NOTE 3 – INVESTMENTS AND DEPOSITS (CONTINUED)**

At June 30, 2018 and 2017, investments were as follows. Investments marked with an asterisk (\*) represent investments exceeding 5% or more of net position available for Plan benefits as of June 30, 2018 and 2017. Investments marked with two asterisks (\*\*) represent international mutual funds.

	<u>2018</u>	<u>2017</u>
<b>Investments:</b>		
Aberdeen Emerging Markets Fund - Institutional Class	\$ 2,616,747 **	\$ 2,664,292 **
EuroPacific Growth Fund® - Class R6	10,681,994 **	9,232,195 **
Dodge & Cox Stock Fund	31,872,924 *	30,880,849 *
DFA U.S. Small Cap Portfolio	12,702,876	12,955,162
The SEI Stable Asset Fund	129,567,328 *	131,884,327 *
Fidelity® Low-Priced Stock Fund - Class K	8,280,812	8,369,432
Fidelity® Diversified International Fund - Class K	11,085,416 **	10,963,620 **
Invesco Global Real Estate - Institutional Class	1,608,850 **	1,639,112 **
Life Cycle 2045 Portfolio	16,405,046	14,249,186
Life Cycle 2035 Portfolio	28,593,392	25,604,863
Life Cycle 2025 Portfolio	49,346,137 *	45,311,209 *
Conservative Portfolio	39,979,984 *	38,187,781 *
Life Cycle 2055 Portfolio	8,026,436	6,066,221
Life Cycle 2020 Portfolio	2,909,595	1,711,248
Life Cycle 2030 Portfolio	3,087,360	1,961,495
Life Cycle 2040 Portfolio	3,391,977	2,348,931
Life Cycle 2050 Portfolio	1,637,973	770,947
Vanguard Inflation Protected Securities Fund-Institutional Shares	4,310,152	5,014,054
Oakmark Equity and Income Fund (The) - Class I	20,893,841	20,506,932
Principal Investors Fund, Inc. - MidCap Blend Fund - Institutional Class	12,898,415	12,304,374
Principal Diversified Real Asset Fund - Institutional Class	452,591	399,070
Templeton Global Bond Fund - Class R6	2,972,907	1,868,902
Fidelity® Contrafund - Class K	49,201,339 *	38,263,005 *
T. Rowe Price Institutional Mid-Cap Equity Growth Fund	30,451,249 *	26,713,104
Vanguard Institutional Index Fund - Institutional Plus Shares	85,059,659	-
Vanguard Institutional Index Fund - Institutional Shares	-	81,346,646 *
Vanguard Total Bond Market Index Fund - Institutional Shares	16,031,820	16,798,883
Vanguard Total International Stock Fund - Institutional Shares	3,460,779 **	2,893,223 **
	<u>587,527,599</u>	<u>550,909,063</u>

**STATE OF NEW MEXICO PUBLIC EMPLOYEES’  
DEFERRED COMPENSATION PLAN  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2018 and 2017**

**NOTE 3 – INVESTMENTS AND DEPOSITS (CONTINUED)**

	<b>2018</b>	<b>2017</b>
<b>Suspense:</b>		
Monies held pending investment	1,150	(108,136)
<b>Payouts:</b>		
Nationwide Fixed Annuity Payout Option (at contract value)	1,062,992	1,197,477
Nationwide Variable Annuity Payout Option	28,774	26,802
<b>Self Directed Option:</b>		
Investments Held at Charles Schwab	4,954,319	4,629,288
<b>Total investments at fair value</b>	<b>\$ 593,574,834</b>	<b>\$ 556,654,494</b>

The Plan has a formal investment policy that allows the Plan to select investment options that offer the best prospects to meet the participant’s financial goals. The Policies allow for different tiers of investments that provide options for the participant to choose from. These are participant directed accounts, thus there are no limitations on concentration, credit and interest rate risk aside from the Plan’s evaluation of the appropriate investment options to offer. The policy and investment offerings are reviewed and evaluated to ensure appropriate funds are available to the participant.

**Custodial credit risk** is the risk that, in the event of a failure of the counterparty, the Plan would not be able to recover the value of its deposits, investments, or collateral securities that were in the possession of an outside party. Investment securities are exposed to custodial credit risk if they are uninsured or not registered in the name of the Plan and are held by either the counterparty or the counterparty’s trust department or agent, but not in the Plan’s name.

Investments in the stable value option are held in the Plan's name by Galliard Capital Management, Inc., agent of the Plan. The remaining investments are held in a trust account for the benefit of the Plan. As a result, the investments of the Plan are not exposed to custodial credit risk.

**Credit risk** is the risk that the Plan will lose money because of the default of the security of the issuer or investment counterparty. The stable value option and the variable earnings mutual funds are unrated.

**Concentration of credit risk** is the risk of loss attributed to the magnitude of the Plan’s investment in a single issuer. The Plan’s investments are managed by several fund managers. The concentrations of investments are determined by the participants’ elections to invest in the available investment options as selected by the Committee. The investments that exceed 5% are indicated in the previous table.

**Foreign currency risk** is the risk that changes in exchange rates could adversely affect the fair value of the investment. The Plan allows the option of investments in mutual funds of countries outside the U.S. that invest in securities not required to disclose the individual assets within the fund. The fair value of these investments was \$29,453,785 and \$27,392,441 as of June 30, 2018 and 2017, respectively. The individual funds are identified in the previous table.

**Interest rate risk** is the risk that changes in interest rates that will adversely affect the value of an investment.

**STATE OF NEW MEXICO PUBLIC EMPLOYEES'  
DEFERRED COMPENSATION PLAN  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2018 and 2017**

**NOTE 3 – INVESTMENTS AND DEPOSITS (CONTINUED)**

As of June 30, 2018, and 2017, the Plan had the following investments and maturities in its fixed earnings investments, stable asset investments and its mutual funds, which include investments in bonds. Weighted average maturities will vary annually based on the underlying investments of funds.

	2018		2017	
	Fair Value	Weighted Average Maturity	Fair Value	Weighted Average Maturity
<b>Stable Value Option:</b>				
Stable Value Fund	\$ 129,567,328	3.45	\$ 131,884,327	3.47
<b>Variable Earnings Investments:</b>				
Life Cycle 2025 Portfolio	49,346,137	1.94	45,311,209	2.41
Life Cycle 2035 Portfolio	28,593,392	1.06	25,604,863	1.44
Life Cycle 2045 Portfolio	16,405,046	0.68	14,249,186	1.10
Life Cycle 2055 Portfolio	8,026,436	1.71	6,066,221	0.94
Life Cycle 2020 Portfolio	2,909,595	2.71	1,711,248	2.88
Life Cycle 2030 Portfolio	3,087,360	1.56	1,961,495	1.92
Life Cycle 2040 Portfolio	3,391,977	0.78	2,348,931	1.23
Life Cycle 2050 Portfolio	1,637,973	1.25	770,947	1.00
Oakmark Equity and Income Fund (The) - Class I	20,893,841	-	20,506,932	-
Vanguard Total Bond Market Index Instl	16,031,820	8.40	16,798,883	8.30
Life Cycle Conservative Portfolio	39,979,984	2.24	38,187,781	3.25
Blackrock Inflation Protected Bond	-	8.83	-	9.92
Templeton Global Bond Fund - Class R6	2,972,907	3.08	1,868,902	3.80

Since all investments are participant directed, all risks exist at the participant level. Each individual within the Plan has the ability to liquidate their positions on demand and has responsibility for managing their exposure to fair value loss.

**NOTE 4 – ALLOCATED LIFE INSURANCE CONTRACTS**

Generally accepted accounting principles require that contracts in a participant's name be excluded from the face of the financial statements. This product was closed to new participants in 2001. The values of insurance contracts change daily due to premiums paid, investment return and settlements of cash surrender value. Due to the actual cash surrender value being significantly less than the policyholder account value in the early years of universal life insurance contracts, a participant may receive substantially less than the value of their account upon the withdrawal of funds from their universal life insurance contract. The total amount of life insurance in force at June 30, 2018 and 2017 was \$11,609,992 and \$12,789,021, respectively. The cash surrender value of policies in force as of June 30, 2018 and 2017 was \$1,457,469 and \$1,559,744, respectively.

#### **NOTE 5 – PLAN ADMINISTRATOR AND ADMINISTRATIVE EXPENSES**

The Plan's third-party administrator is Nationwide Retirement Solutions, Inc. (NRS). For services performed, NRS receives an annual per participant account administrative fee; this fee is charged at an average cost of \$7.50 per quarter plus .135% of assets, not to exceed \$26 per quarter, per participant. NRS and Nationwide are subsidiaries of Nationwide Financial Services, Inc. In fiscal year 2017 NRS received an annual per participant account of \$13.00 per quarter per participant.

The Plan's independent investment consultant is Meketa Investment Group (MIG). For services performed by MIG an annual fee is charged at an average cost of \$1.02 per quarter per participant. In fiscal year 2017 the annual fee was at an average cost of \$1.13 per quarter per participant.

The New Mexico Public Employees Retirement Association (PERA) receives an annual per participant fee to cover the direct expenses of administering the Plan; this fee is charged at an average cost of \$1.00 per quarter per participant. In fiscal year 2017 the fee was at an average cost of \$1.06 per quarter per participant.

NRS charges an initial set-up fee of \$50 and an annual maintenance fee of \$50 on each participant self-directed brokerage account. Charles Schwab may assess a charge on transfers related to participant self-directed brokerage accounts. NRS charges an annual loan maintenance fee of \$50. There is also the possibility of an annual loan default fee of \$50 and an insufficient funds fee of \$25. Another optional service available to Plan participants is Morningstar Advice Online. A \$45 annual fee is charged to participant's using this service.

#### **NOTE 6 – TAX STATUS**

In the opinion of the legal counsel, the Plan is an eligible deferred compensation plan as defined by Section 457 to the IRC. Accordingly, any amount of compensation deferred under the Plan and any income attributable to the amounts so deferred shall be included in the gross income of the participant only for the taxable year in which such compensation or other income is paid or, otherwise, made available to the participant or their beneficiary.

#### **NOTE 7 – RISKS AND UNCERTAINTIES**

The Plan invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect participants' account balances and the amounts reported in the Statements of Plan Net Position.

#### **NOTE 8 – RELATED PARTIES**

Certain Board members of the Public Employees' Retirement Association are active participants in the Plan.

**SUPPLEMENTARY INFORMATION**

**STATE OF NEW MEXICO PUBLIC EMPLOYEES'  
DEFERRED COMPENSATION PLAN  
SCHEDULE OF MEMORANDUMS OF UNDERSTANDING  
Year Ended June 30, 2018**

<b><i>Participants</i></b>	<b><i>Party Responsible for Operations</i></b>	<b><i>Beginning and Ending Dates</i></b>	<b><i>Total Estimated Amount of Project</i></b>	<b><i>Portion Applicable to the Agency</i></b>	<b><i>Amount Agency Contributed in the Current Fiscal Year</i></b>	<b><i>Audit Responsibility</i></b>	<b><i>Fiscal Agent</i></b>	<b><i>Government Agency Where Revenues and Expenditures are Reported</i></b>
Nationwide Retirement Solutions, Inc. Public Employees Retirement Board	Nationwide Retirement Solutions, Inc.	October 1, 2011 through September 30, 2019	Annual fee assessed quarterly \$45-\$52 per participant account	\$ -	\$ -	Nationwide Retirement Solutions, Inc.	N/A	State of New Mexico Deferred Compensation Plan

See Independent Auditor's Report





**Independent Auditor’s Report 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***

Investment Committee and PERA Board Members  
The State of New Mexico Public Employees’  
Deferred Compensation Plan

We have audited, 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, the financial statements of the State of New Mexico Public Employees’ Deferred Compensation Plan (the Plan) as of and for the year ended June 30, 2018, and have issued our report thereon dated October 25, 2018.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the State of New Mexico Public Employees' Deferred Compensation Plan'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 the State of New Mexico Public Employees' Deferred Compensation Plan’s internal control. Accordingly, we do not express an opinion on the effectiveness of the State of New Mexico Public Employees' Deferred Compensation Plan’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 over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not yet been identified.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the State of New Mexico Public Employees' Deferred Compensation Plan'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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

## **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 results 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.

A handwritten signature in cursive script that reads "Eide Bailly LLP". The signature is written in black ink and is positioned above the printed name and date.

Boise, Idaho  
October 25, 2018

**STATE OF NEW MEXICO PUBLIC EMPLOYEES'  
DEFERRED COMPENSATION PLAN  
SCHEDULE OF OFFICIALS ROSTER  
June 30, 2018**

Mr. James Maxon	Chair	County Member
Ms. Jackie Kohlasch	Vice-Chair	State Member
Ms. Cathy Townes		State Member
Ms. Claudia Armijo		State Member
Ms. Natalie Cordova		State Member
Ms. Patricia French		Municipal Member
Mr. Dan Esquibel		Municipal Member
Mr. John Melia		Municipal Member
Mr. Daniel Mayfield		Retiree Member
Ms. Loretta Naranjo-Lopez		Retiree Member
Ms. Maggie Toulouse Oliver	Ex-Officio	Secretary of State
Mr. Tim Eichenberg	Ex-Officio	State Treasurer

**STATE OF NEW MEXICO PUBLIC EMPLOYEES'  
DEFERRED COMPENSATION PLAN  
SCHEDULE OF EXIT CONFERENCE ATTENDEES  
June 30, 2018**

The exit conference was held on October 25, 2018 in a closed executive session and was attended by the following individuals:

**Members Present:**

James Maxon	Board Chair	Municipal Member
Jackie Kohlasch	Vice Chair	State Member
Natalie Cordova		State Member
Claudia Armijo		State Member
John Melia		Municipal Member
Loretta Naranjo Lopez		Retiree Member
Dan Mayfield		Retiree Member

**Members Excused:**

Patricia French		Municipal Member
Dan Esquibel		State Member
Cathy Townes		State Member
Maggie Toulouse-Oliver		Ex-officio Member
Tim Eichenberg		Ex-officio Member

**Eide Bailly LLP**

Brad Berls - Partner