

**Virginia**  
**Pooled OPEB Trust Fund**

Comprehensive Annual Financial Report  
For the Year Ended June 30, 2016

# Virginia Pooled OPEB Trust Fund

Comprehensive Annual Financial Report

For the Year Ended June 30, 2016



Prepared by:

VML/VACO Finance

**Virginia Pooled OPEB Trust Fund  
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# Virginia Pooled OPEB Trust Fund

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## *Letter of Transmittal*

November 16, 2016

Honorable Board of Trustees  
Virginia Pooled OPEB Trust Fund  
Richmond, Virginia

It is our pleasure to submit the *Comprehensive Annual Financial Report* (CAFR) of the Virginia Pooled OPEB Trust Fund (Trust) for the year ended June 30, 2016. The CAFR represents a compilation of financial data that details the Trust's financial status. Information contained in this report was prepared in strict conformance with accounting principles generally accepted in the United States of America as promulgated by the Government Accounting Standards Board (GASB). The CAFR is intended to provide readers with a clearly articulated, user-friendly reporting of the Trust's financial affairs. Responsibility for both the accuracy of the data, and the completeness and reliability of the presentation, including all disclosures, rests with the management of the Trust. To the best of our knowledge and belief, the enclosed data are accurate in all material respects and are reported in a manner that presents fairly the financial position and the activities of the Trust.

The CAFR is presented in three sections:

- 1) *Introductory Section* – includes this letter of transmittal, identification of the Trust's administrative organization, and descriptions of administrative responsibilities.
- 2) *Financial Section* – consists of the Report of Independent Auditors, Management's Discussion and Analysis (MD&A), basic financial statements, and the notes to the financial statements.
- 3) *Compliance Section* – consists of the Report of Independent Auditor 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.

Management's Discussion and Analysis (MD&A) immediately follows the independent auditor's report and provides a narrative introduction, overview, and analysis of the basic financial statements. MD&A complements, and should be read in conjunction with, this letter of transmittal.

## ***Background***

The Virginia Pooled OPEB Trust Fund, operating pursuant to the Virginia Pooled OPEB Trust Fund Agreement, was established on April 11, 2008, as an irrevocable trust to receive, invest, and disburse funds set aside by political subdivisions of the Commonwealth of Virginia to defray future expenses related to post-employment benefits other than pensions (OPEB). Income of the Trust is tax-exempt under Section 115 of the Internal Revenue Code. The Trust is jointly sponsored by the Virginia Association of Counties (VACo) and the Virginia Municipal League (VML) and operates as the “VACo/VML Pooled OPEB Trust.” Primary benefits of participation in the Trust include professional management of trust assets in two diversified investment portfolios: one with a targeted rate of return of 7.5% and the other with a targeted rate of return of 6.5%. Participants hold individual trust accounts wherein they can monitor the performance of their investments without the burden and expense of directing privately managed individual trust accounts.

As of June 30, 2016, the Trust held 47 employer accounts for Virginia political subdivisions and related governmental entities. In some cases, related employers, such as a primary government and its public school system, have established joint Trust accounts.

The Virginia Local Government Finance Corporation (VLGFC), operating as “VML/VACo Finance,” provides day-to-day administration of the Trust pursuant to a Memorandum of Agreement. An investment consultant is retained by the Trust to provide ongoing investment advice to the trustees. A custodian bank has also been contracted to assist with the management of assets and the reporting of contributions, distributions and employer balances within the Trust.

## ***FY 2016 Highlights***

Fiscal Year 2016 saw continued growth for the Virginia Pooled OPEB Trust. The net position of the Trust increased substantially during the year, growing from \$757 million on June 30, 2015, to \$812 million on June 30, 2016.

The Board of Trustees focused its efforts on the Trust’s performance and took several steps with the aim of improving the likelihood of achieving its targeted rates of return. In September 2015, the Board approved a 5% allocation to private equity for Portfolio I. The Trustees committed \$12.9 million to the Warburg Pincus Private Equity XII Fund, a thesis-driven growth fund investing at all stages of a company’s life. In May 2016, the Board approved an allocation of 2% (Portfolio I) and 1% (Portfolio II), respectively, to opportunistic real estate and selected UBS to manage the investment. This investment will replace the Trust’s investment in the SPDR Dow

Jones Global Real Estate ETF. The investment in UBS’s Trumbull Property Growth & Income Fund is subject to capital calls. The first \$7 million of the Trust’s \$18 million commitment to UBS was called in October 2016.

The Trust redeemed its investment with its emerging markets equity manager, Vontobel Asset Management, following the departure of key personnel. The proceeds of the redemption were invested in the Vanguard Emerging Markets ETF until a replacement manager could be selected. Alliance Bernstein was subsequently selected to replace Vontobel at the Board of Trustees meeting held on September 9, 2016.

### ***Summary of Financial Condition***

The objective of the Trust is to assist participating employers in providing for their OPEB obligations by generating investment earnings on employer contributions. Individual participants engage their own consulting actuaries to determine their long-term OPEB obligations and the sufficiency of current contribution levels to fund the liabilities of each plan over a reasonable time frame. Contributions not necessary for the payment of current expected benefits may be remitted to the Trust for long-term investment. Governmental accounting standards specify that the maximum acceptable amortization period for the total unfunded actuarial liability is 30 years.

An optimally diversified investment portfolio is designed to provide long-term returns for a given level of risk as measured by volatility. Portfolio I is designed to produce an expected rate of return of 7.5%; Portfolio II has an expected rate of return of 6.5%. For the period ended June 30, 2016, Portfolio I produced an actual one-year return of -0.22% and a three-year annualized return of 4.75%. Portfolio II, which was established on September 30, 2009, produced an actual one-year return of 1.72% and a three-year annualized return of 4.48%.

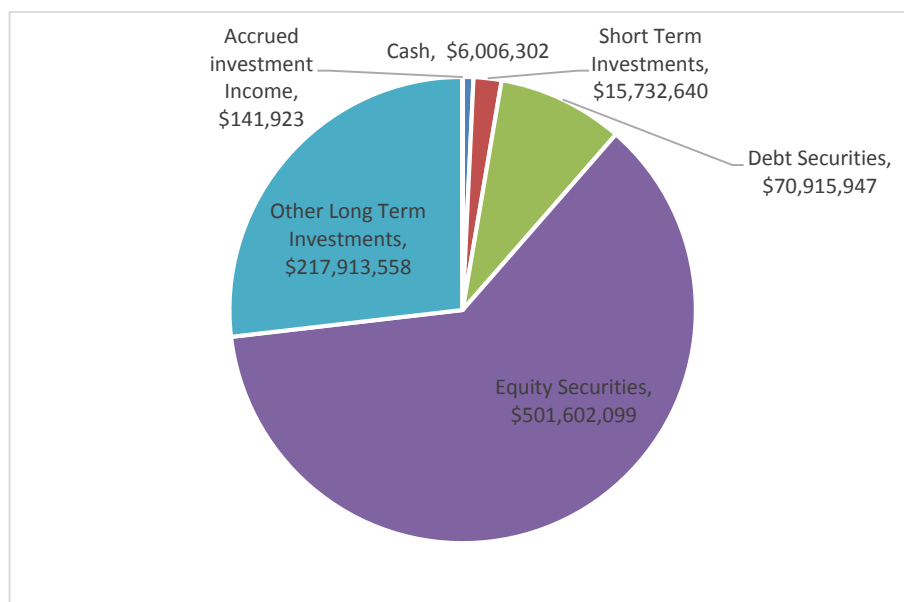
The Trust measures its returns against a customized benchmark, composed of recognized indexes for each asset class weighted by the Trust's target allocation for that asset class. For example, 26.0% of Portfolio I's custom benchmark is composed of the return of the Russell 1000. For the year ended June 30, 2016, the custom benchmark for Portfolio I returned a one-year and three-year annualized return of -0.44% and 5.44%, respectively, whereas the custom benchmark for Portfolio II returned a one year and three-year annualized return of 2.35% and 5.03%, respectively.

The target allocations of the Trust as of June 30, 2016, were as follows:

<b>Asset Class</b>	<b>Portfolio I</b>	<b>Portfolio II</b>
<b>Total Equity</b>	<b>59.0%</b>	<b>32.0%</b>
Large Cap Equity	26.0%	15.0%
Small Cap Equity	10.0%	6.0%
International Equity	13.0%	8.0%
Emerging Markets Equity	5.0%	3.0%
Private Equity	5.0%	0.0%
<b>Fixed Income</b>	<b>21.0%</b>	<b>58.0%</b>
Core Plus	14.0%	40.0%
Core	7.0%	18.0%
<b>Diversified Hedge Funds</b>	<b>10.0%</b>	<b>5.0%</b>
<b>Real Assets</b>	<b>10.0%</b>	<b>5.0%</b>
Real Estate	7.0%	3.0%
Commodities	3.0%	2.0%
<b>Cash &amp; Equivalents</b>	<b>0.0%</b>	<b>0.0%</b>

The target allocations are updated and revised as needed by the Board of Trustees with the advice of an investment advisor.

### Value of Investments by Asset Allocation as of June 30, 2016



#### ***Independent Audit***

For the year ended June 30, 2016, the Trust's financial statements were audited by the certified public accounting firm of Dixon Hughes Goodman LLP to provide reasonable assurance that the financial statements of the Trust were free of material misstatement. The audit: a) examined activities, documents, and disclosures used to create the financial statements, b) assessed the accounting principles used by management, and c) evaluated the overall financial statement presentation.

#### ***Acknowledgements***

The completion of this report reflects the efforts of the Board of Trustees and staff of VML/VACo Finance working together to achieve the goals of the Trust. The report is intended to provide comprehensive and reliable information about the Trust and allow for the evaluation of responsible stewardship of the funds of the Trust's net assets.

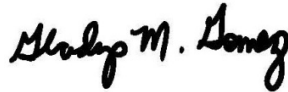


We express our gratitude to the members of the Board, the consultants, the auditors, and the many people who have worked so diligently to assure the successful operation of the Trust.

Respectfully submitted,



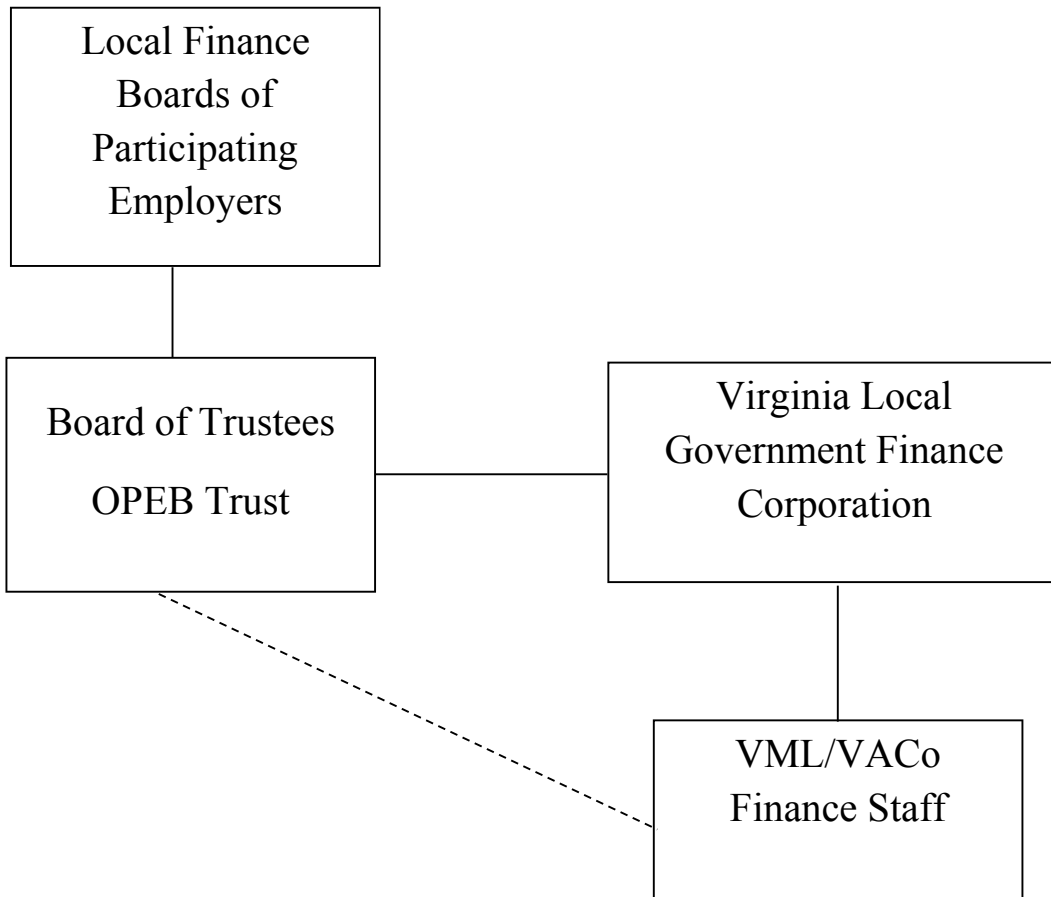
Robert W. Lauterberg  
Managing Director  
VML/VACo Finance



Gladys M. Gomez, CPA, CGMA  
Comptroller  
VML/VACo Finance

# Virginia Pooled OPEB Trust Fund

## Organization Chart



**Virginia Pooled OPEB Trust Fund**  
**Governing Board and Administration**  
**June 30, 2016**

**Board of Trustees**

Richard A. Cordle, Chairman  
Treasurer  
County of Chesterfield

Susan S. Quinn, Vice Chairman  
Chief Operating Officer  
Fairfax County Public Schools

Kevin S. Boggess  
City Manager  
City of Salem

Patricia A. Phillips  
Director of Finance  
City of Virginia Beach

Laura M. Rudy  
Treasurer  
County of Stafford

Eugene H. Walter  
Director of Finance  
County of Henrico

Jeffrey Weiler  
Executive Director  
Fairfax County Retirement Boards

Lance W. Wolff  
Assistant Superintendent for Financial Services  
Stafford County Public Schools

H. Roger Zurn, Jr.  
Treasurer  
Loudoun County

**Administrative Staff**

Robert W. Lauterberg  
Managing Director  
VML/VACo Finance

Steven C. Mulroy  
Deputy Director  
VML/VACo Finance

Gladys M. Gomez, CPA, CGMA  
Comptroller  
VML/VACo Finance

**Investment Consultant**

Asset Consulting Group, LLC  
St. Louis, Missouri

**Custodian**

Comerica Bank, Inc.  
Detroit, Michigan



## **Independent Auditors' Report**

Board of Trustees  
Virginia Pooled OPEB Trust Fund

### **Report on the Financial Statements**

We have audited the accompanying financial statements of Virginia Pooled OPEB Trust Fund, which comprise the statement of net position and the related statement of changes in net position, as of and for the year ended June 30, 2016, and the related notes to the financial statements.

### **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 audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 net position of the Virginia Pooled OPEB Trust Fund as of June 30, 2016, and the respective changes in financial position for the year ended June 30, 2016, in accordance with accounting principles generally accepted in the United States of America.

### **Required Supplementary Information**

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 12 through 16 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 an opinion on the financial statements that collectively comprise the Virginia Pooled OPEB Trust Fund's basic financial statements. The introductory section is presented for purposes of additional analysis and is not a required part of the basic financial statements. The introductory section has not been subjected to the auditing procedures applied on 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 November 16, 2016, on our consideration of the Virginia Pooled OPEB Trust Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to prove 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 Virginia Pooled OPEB Trust Fund's internal control over financial reporting and compliance.

*Dixon Hughes Goodman LLP*

**Richmond, Virginia  
November 16, 2016**

## ***Virginia Pooled OPEB Trust***

### ***Management's Discussion and Analysis***

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#### **For the Year Ended June 30, 2016**

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Management offers the following discussion and analysis as a narrative introduction to the basic financial statements and an analytical overview of the Trust's financial activities for the fiscal year ended June 30, 2016. This narrative is intended as a supplement and should be read in conjunction with the financial statements.

#### ***Overview of the Financial Statements***

The Trust's financial statements include the following components:

- Statement of Net Position
- Statement of Changes in Net Position
- Notes to Financial Statements

The *Statement of Net Position* presents the Trust's assets and liabilities and the resulting net assets, which are held in trust for the other postemployment benefits of contributing members. This statement reflects a year-end snapshot of the Trust's investments, at fair value, along with cash and short-term investments, receivables and other assets and liabilities.

The *Statement of Changes in Net Position* presents information showing how the Trust's net assets held in trust for other postemployment benefits changed during the period. This statement includes additions for contributions by employers and investment earnings and deductions for payments, refunded contributions and administrative expenses.

The *Notes to Financial Statements* are an integral part of the financial statements and provide additional information that is necessary in order to gain a comprehensive understanding of data reported in the financial statements.

#### ***Financial Highlights***

- Net position is restricted for future benefit payments of participating localities. Net position at June 30, 2016, totaled \$812 million.
- Outstanding accounts payable at year end were \$511,278. This amount represents fees payable to the program administrator and fund managers.
- The net increase in net assets was \$55 million including employer contributions of \$63 million with one participant withdrawal of \$9.1 million.

***Condensed Financial Information***

In order to ensure the ability of participating employers to properly fund the payment of other postemployment benefits for their employees in future years, it is advisable for employers to accumulate funds on a regular and systematic basis. The principal sources from which the Trust derives additions are employer contributions and earnings on investments.

Comparative summary financial statements of the Trust are presented as follows:

**NET POSITION  
June 30, 2015 and 2016**

	<b>2015</b>	<b>2016</b>
<b>ASSETS</b>		
Cash	\$ 7,145,502	\$ 6,006,302
Short Term Investments	19,149,952	15,732,640
Long Term Investments	730,973,809	790,431,604
Accrued investment Income	274,891	141,923
<b>TOTAL ASSETS</b>	<b>\$ 757,544,155</b>	<b>\$ 812,312,469</b>
<b>LIABILITIES</b>		
Accounts payable	\$ 511,919	\$ 511,278
<b>TOTAL LIABILITIES</b>	<b>\$ 511,919</b>	<b>\$ 511,278</b>
<b>NET POSITION RESTRICTED FOR OPEB</b>	<b>\$ 757,032,236</b>	<b>\$ 811,801,191</b>



**CHANGES IN NET POSITION**  
**Years Ended June 30, 2015 and 2016**

	<b>2015</b>	<b>2016</b>
<b>ADDITIONS</b>		
Employer contributions	\$ 70,009,069	\$ 63,216,531
Net investment income	14,738,596	1,354,385
<b>TOTAL ADDITIONS</b>	<b>\$ 84,747,665</b>	<b>\$ 64,570,916</b>
<b>DEDUCTIONS</b>		
Professional Services, Investment Advisory, and Administration	\$ 703,612	\$ 701,961
Participant Withdrawal	-	9,100,000
<b>TOTAL DEDUCTIONS</b>	<b>\$ 703,612</b>	<b>\$ 9,801,961</b>
<b>NET CHANGE</b>	<b>\$ 84,044,053</b>	<b>\$ 54,768,955</b>
<b>NET POSITON</b>		
<b>BEGINNING OF YEAR</b>	<b>\$ 672,988,183</b>	<b>\$ 757,032,236</b>
<b>END OF YEAR</b>	<b>\$ 757,032,236</b>	<b>\$ 811,801,191</b>

***Analysis of Financial Position and Results of Operations***

The Trust's net position was \$812 million at June 30, 2016. Related employers, such as a primary government and a school system, may join the Trust individually or as one participant. During FY2016, contributions were made to thirty of the forty-seven participant accounts. Among these, the City of Fredericksburg, York County and York County Public Schools, made their initial contributions during FY 2016.

Current Trust participants and the fiscal year in which they joined the Trust are as follows:

Henrico County	2007-2008
City of Suffolk & City of Suffolk Public Schools	2007-2008
Fairfax County	2007-2008
City of Chesapeake Public Schools	2007-2008
Chesterfield County, Chesterfield County Public Schools, & Chesterfield County Line of Duty Act	2007-2008
City of Roanoke & City of Roanoke Line of Duty Act	2007-2008
Fairfax County Public Schools	2007-2008
City of Virginia Beach & Virginia Beach Public Schools	2007-2008
Health Care Commission of Chesterfield County	2008-2009
Stafford County Public Schools	2008-2009
Fauquier County & Public Schools	2008-2009
Town of Leesburg	2008-2009
City of Staunton & Staunton City Public Schools	2008-2009
Newport News Redevelopment & Housing Authority	2008-2009
Southeastern Cooperative Educational Programs	2008-2009
Richmond Metropolitan Authority	2008-2009
Henry County, Henry County Schools, Henry County Social Services, & Henry County PSA	2008-2009
Roanoke County & Roanoke County Public Schools	2008-2009
Stafford County	2008-2009
Town of Blacksburg	2008-2009
Alexandria City Public Schools	2008-2009
City of Salem & Salem City Schools	2008-2009
Fluvanna County	2008-2009
Rappahannock Area Community Services Board	2009-2010
Loudoun County & Loudoun County Public Schools	2009-2010
Newport News Public Schools	2009-2010
Town of Ashland	2010-2011
Mecklenburg County	2010-2011

Spotsylvania County Public Schools	2011-2012
City of Lexington & Public Schools	2011-2012
Loudoun Water	2012-2013
Alexandria Renew Enterprises	2013-2014
Accomack County	2014-2015
City of Fredericksburg	2015-2016
York County and York County Public Schools	2015-2016

***Requests for Information***

This financial report is designed to provide a general overview of the Trust's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to:

Managing Director  
VML/VACo Finance  
919 E. Main St., Suite 1100  
Richmond, VA 23219  
(804) 648-0635

*Virginia Pooled OPEB Trust*

*Statement of Net Position*

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	<u>June 30, 2016</u>
<b>ASSETS</b>	
Cash	\$ 6,006,302
Short Term Investments	15,732,640
Long Term Investments at fair value	
Debt Securities	70,976,697
Equity Securities	501,541,349
Other Long Term Investments	217,913,558
Accrued investment income	<u>141,923</u>
	<u>812,312,468</u>
 <b>LIABILITIES</b>	
Accounts payable	<u>511,277</u>
 <b>NET POSITION RESTRICTED FOR OPEB</b>	 <u>\$ 811,801,191</u>

*The accompanying notes are an integral part of these financial statements.*

*Virginia Pooled OPEB Trust*

*Statement of Changes in Net Position*

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	<b>Year Ended June 30, 2016</b>
<b>ADDITIONS</b>	
Employer contributions	\$ 63,216,531
Investment income	
Net depreciation in fair value of investments	(4,364,217)
Interest and dividends	8,049,377
Less investment expenses	(2,330,775)
	<u>1,354,385</u>
<b>TOTAL ADDITIONS</b>	<u>64,570,916</u>
<b>DEDUCTIONS</b>	
Professional services, investment advisory & administrative	701,961
Participant Withdrawal	<u>9,100,000</u>
	<u>9,801,961</u>
<b>NET CHANGE</b>	54,768,955
<b>NET POSITION:</b>	
<b>BEGINNING OF YEAR</b>	<u>757,032,236</u>
<b>END OF YEAR</b>	<u>\$ 811,801,191</u>

*The accompanying notes are an integral part of these financial statements.*

## *Virginia Pooled OPEB Trust*

### *Notes to Financial Statements*

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**June 30, 2016**

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#### **1. Organization and Nature of Activities**

The Virginia Pooled OPEB Trust Fund (Trust) was established April 11, 2008, for the purpose of accumulating and investing assets to fund post-employment benefits other than pensions for counties, cities, towns, school divisions and other authorized political subdivisions of the Commonwealth of Virginia. The Trust is not a component unit of another governmental entity.

The Trust's Board of Trustees has fiduciary responsibility for the investment of monies and administration of the Trust pursuant to the Trust Agreement. The Board of Trustees is currently composed of nine members. Trustees are members of Local Finance Boards of participating employers and are elected for staggered three-year terms by the participants in the Trust.

The Trust does not purport to present the financial status of each of the participating employer's post-employment benefit plans, nor do these statements contain information on accumulated plan benefits and other disclosures necessary for a fair presentation of the individual plan in accordance with accounting principles generally accepted in the United States of America.

#### **2. Summary of Significant Accounting Policies**

##### **Measurement Focus and Basis of Accounting**

The financial statements of the Trust are presented as a fiduciary fund type. The economic resources measurement focus and the accrual basis of accounting are used in the preparation of the financial statements. Employer contributions to each plan are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each employer's plan.

##### **Cash and Cash Equivalents**

The Trust considers all cash and highly liquid investments with original maturities of three months or less to be cash equivalents. All cash equivalents are recorded at cost, which approximates fair value.

##### **Investments**

Investments are reported at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. See Note 3 and Note 4 for discussion of fair value measurements. Net investment income consists of realized and unrealized appreciation (depreciation) in the fair value of investments, interest income earned, and investment expense. Realized gains and losses on the sale of investments are recognized on the specific identification basis to determine the cost basis of the investments sold.

In order to account for each participating employer's activity, separate accounts are maintained by the Trust. As such, investment and expenses are separately accounted for and maintained by employers.

## **Taxes**

The Trust is exempt from taxation under Section 115 of the Internal Revenue Code. Accordingly, the accompanying financial statements do not include a provision for federal or state income taxes.

## **Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements. Such estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates and assumptions.

## **Termination**

The Trust Agreement specifically allows for the termination of the Trust once “all participation interests of all participating employers have been terminated in their entirety.” Partial termination would occur when a participating employer’s interest in the Trust is terminated or when a Trust Joinder Agreement has been terminated. In case of termination, either in whole or in part, affected assets of the Trust are distributed or transferred in accordance with the Trust Agreement to a trust or trusts established by the participating employer(s) for the funding of other postemployment benefits.

## **Subsequent events**

In preparing these financial statements, the Trust has evaluated events and transactions for potential recognition or disclosure through November 16, 2016, the date the financial statements were available to be issued.

### **3. Investments and Risk**

The following information regarding disclosures of credit and interest rate risk are designed to inform financial statement users about investment risks which could affect the Trust’s ability to meet its obligations. The standard of prudence to be used by investment officials of the Trust shall be the “prudent person” and shall be applied in the context of managing the portfolios.

#### **Custodial Credit Risk – Deposits**

The Virginia Security for Public Deposits Act (Act) requires financial institutions holding public deposits in excess of amounts covered by federal insurance to pledge collateral to a pool in the name of the State Treasury Board. The State Treasury Board is responsible for monitoring compliance with the requirements of the Act and for notifying local governments of compliance by banks and savings and loans. If the value of the pool’s collateral is inadequate to cover a loss, additional amounts would be assessed on a pro rata basis to the members of the pool. Accordingly, all deposits in banks and savings and loans are considered to be insured. The Trust had no carrying amount or bank balance on deposit at June 30, 2016.

### **Interest Rate Risk – Investments**

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in interest rates.

### **Foreign Currency Risk – Investments**

The Trust's exposure to foreign currency risk derives from its holdings of foreign securities and the use of derivatives to hedge the related foreign currency exposure back to the U.S. dollar. Sources of foreign currency risk include the Trust's investments in international equities, emerging markets equities, and fixed income securities. The Trust's international equity, emerging market equity, and fixed income portfolios are currently implemented through commingled funds. The managers of these commingled funds are expected to prudently diversify the portfolios. Commingled fund assets are expected to be managed within the guidelines set forth for each fund by the manager.

### **Credit Risk - Investments**

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to the Trust. Credit risk is measured by the assignment of a rating by a nationally recognized statistical rating organization. Obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk and disclosure is not required.

### **Concentration of Credit Risk - Investments**

Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The Trust's fixed income investments are currently implemented through commingled funds. Commingled fund assets are expected to be managed within the guidelines set forth for each fund by the manager. Managers of these funds are expected to maintain appropriate levels of diversification in the portfolios.

## **4. Fair Value Measurements**

Fair value, as defined under GAAP, is an exit price representing the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. GAAP establishes a three-tier fair value hierarchy which prioritizes the inputs used in measuring fair value. These tiers include:

- Level 1: Observable inputs such as quoted prices in active markets.
- Level 2: Inputs other than quoted prices in active markets that are either directly or indirectly observable.
- Level 3: Unobservable inputs about which little or no market data exists, therefore requiring an entity to develop its own assumptions.



Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The Trust's assessment of the significance of a particular input to the fair value measurement requires judgment, and may affect the valuation of fair value assets and liabilities and their placement within the fair value hierarchy levels.

There have been no changes in the methodologies used June 30, 2016. The following is a description of the valuation methodologies used for assets measured at fair value:

***Common Stocks***

Common stocks in the Trust are publicly traded investments, and are valued daily at the closing price reported on the active market on which the individual securities are traded.

***Mutual Funds***

Mutual funds are publicly traded investments and are valued daily at the closing price reported on the active market on which the funds are traded.

***Exchange Traded Funds (ETFs)***

ETFs are publicly traded investments and are valued daily at the closing price reported on the active market on which the funds are traded.

***Commingled Accounts***

The Trust invests in commingled accounts for which quoted prices are not available in active markets for identical instruments. The Trust utilizes the NAV per share, as determined by the respective investment manager, as the estimated fair value. Because quoted prices in active markets for identical assets are not available, these prices are determined using observable market information such as quotes from less active markets and/or quoted prices of securities with similar characteristics.

***Limited Partnership – Fund of Hedge Funds***

This fund invests in a number of underlying hedge funds which pursue various strategies. The strategies pursued by the underlying hedge funds include: credit, equity, macro, multi-strategy, and relative value. The Trust's interest in the fund is valued at the NAV of units of the collective partnership. The NAV is used as a practical expedient to estimate fair value. This practical expedient would not be used if it is determined to be probable that the Trust could not redeem its investment at the NAV per unit reported by the fund. Participant purchases may occur monthly. Redemptions are available quarterly upon 70 days' notice.

***Limited Partnership – Private Equity***

This fund invests in the equity of a variety of privately held companies. The Trust's interest in the fund is valued at the Trust's ownership interest in the collective limited partners' capital. The Trust's ownership interest in limited partners' capital is used as a practical expedient to estimate fair value. This investment can never be redeemed with the fund. Instead, the nature of investments of this type is that distributions are received through the liquidation of the underlying assets of the fund. It is expected that the underlying assets of the fund will be liquidated over a period of six to twelve years. It is probable that the Trust's investment in this fund will be sold at an amount different from Trust's ownership interest in limited partners' capital as of June 30, 2016. The effective date of this fund is December 1, 2015, and it made its inaugural investment in the same month. Barring unusual circumstances the fund values recent investments in nonmarketable securities at acquisition cost. The primary valuation methodology used to determine the fair value of the fund's investments at June 30, 2016, was recent arms-length financing rounds in which the partnership or other partnerships managed by the general partner had participated. As of June 30, 2016, all underlying investments of the fund were valued at cost.

**Partnership – Real Estate**

This fund invests primarily in commercial, industrial, and multi-family residential properties and is valued at the NAV of units of the collective partnership. The NAV is used as a practical expedient to estimate fair value. This practical expedient would not be used if it is determined to be probable that the Trust could not redeem its investment at the NAV per unit reported by the fund. The real estate partnership provides quarterly valuations to the Trust. Individual properties are valued internally by the investment manager quarterly. Internal valuations are completed using valuation techniques such as income capitalization, sales comparison, and cost approaches. Independent external appraisals are generally completed annually. Redemptions are available quarterly upon 45 days' notice.

	Fair Value as of June 30, 2016			
	Level 1	Level 2	Level 3	Total
Mutual funds				
Large cap	\$ 97,303,166	\$ -	\$ -	\$ 97,303,166
Bond	150,014,388	-	-	150,014,388
Exchange traded funds				-
Emerging markets	41,715,845	-	-	41,715,845
Real Estate	20,781,808	-	-	20,781,808
Commingled Accounts				-
International	-	95,015,020	-	95,015,020
Bond	-	77,080,906	-	77,080,906
Commodities	-	15,688,427	-	15,688,427
Partnerships				-
Real Estate	-	-	32,508,312	32,508,312
Limited Partnerships				-
Hedge Funds	-	-	71,854,105	71,854,105
Private Equity	-	-	814,235	814,235
Common Stock				-
Large cap	110,664,589	-	-	110,664,589
Small cap	76,990,803	-	-	76,990,803
Cash & equivalents	21,738,942	-	-	21,738,942
<b>Total</b>	<b>\$ 519,209,540</b>	<b>\$ 187,784,353</b>	<b>\$ 105,176,652</b>	<b>\$ 812,170,545</b>

The Trust recognizes transfers between the levels as of the actual date of the event or change in circumstances that caused the transfer. There were no transfers between levels during the year ended June 30, 2016.

The following table illustrates the activity of Level 3 assets measured at fair value on a recurring basis from June 30, 2015 to June 30, 2016:

	<b>Real Estate Fund</b>	<b>Hedge Funds</b>	<b>Private Equity</b>	<b>Total</b>
Fair value at June 30, 2015	\$ 27,430,561	\$ 71,949,783	\$ -	\$ 99,380,344
Realized gains (losses)	-	-	-	-
Unrealized gains (losses)	1,835,452	(3,768,619)	(88,765)	2,021,933
Purchases	1,302,081	3,252,295	903,000	5,457,376
Pending Trades	(341,683)	(457,888)	-	(799,571)
Settlements	2,281,901	878,534	-	3,160,435
Fair value at June 30, 2016	<u>\$ 32,508,312</u>	<u>\$ 71,854,105</u>	<u>\$ 814,235</u>	<u>\$105,176,652</u>

The following table summarizes investments for which fair value is measured using the NAV per share practical expedient as of June 30, 2016.

	<b>Fair Value at June 30, 2016</b>	<b>Unfunded Commitments</b>	<b>Redemption Frequency (If Currently Eligible)</b>	<b>Redemption Notice Period</b>
International Equity – Baring (a)	\$ 50,466,662	\$ -	Monthly	10 business days
International Equity – Marathon (b)	44,548,358	-	Monthly	5 days
Bonds – Pioneer (c)	77,080,906	-	Monthly	5 days
Fund of Hedge Funds – Grosvenor (d)	72,828,317	-	Quarterly	70 days
Real Estate – AEW (e)	32,508,312	-	Quarterly	45 days
Commodities – Tap Fund (f)	15,688,427	-	Monthly	5 days
Real Estate - UBS TPG (g)	-	18,015,000	Quarterly	60 days
Private Equity - Warburg Pincus (h)	814,235	11,997,000	Not Eligible	N/A
<b>Total</b>	<u>\$ 293,935,217</u>	<u>\$ 30,012,000</u>		

- (a) The Baring Focused International Equity Fund seeks to achieve long term capital appreciation by investing in a minimum of 30 issuers, under normal market conditions, which are organized, headquartered, or domiciled in any country included in the Morgan Stanley Capital International Europe Australasia Far East Index (the “EAFE Index”). Issuers may also include those whose principal listing is on a securities exchange in any country included in the EAFE index. Under normal market conditions, the Fund invests a minimum of 90% of its total assets in equity securities. Redemptions are available monthly upon 10 business days’ notice
- (b) Marathon’s philosophy is focused on the capital cycle approach to investment. This is based on the idea that the prospect of high returns will attract excessive capital and vice versa. This philosophy is intrinsically contrarian and the investment ideas are generally very long-term. Marathon invests in developed international equity markets and seeks to outperform the MSCI EAFE Index over a complete market cycle (generally 3-5 years). Redemptions are available monthly upon 5 days’ notice.
- (c) The Pioneer Institutional Opportunistic Core Plus Portfolio seeks to substantially outperform the Barclays U.S. Universal Index and a peer group of competing managers without incurring significantly higher risk (volatility). The Portfolio seeks to achieve this objective by actively managing a well-diversified portfolio of U.S. and international investment grade and non-investment grade debt securities. Redemptions are available semi-monthly upon 5 days’ notice.
- (d) Grosvenor Institutional Partners is a globally diversified, multi-strategy, multi-manager portfolio that allocates its assets to hedge fund managers that invest in various alternative investment strategies. These underlying managers and strategies may include long and short positions in equity and fixed income securities. Redemptions are available quarterly upon 70 days’ notice.
- (e) The objective of the AEW Core Property Trust (U.S.) Fund is to invest in core real estate assets that will provide investors with a targeted net return that will exceed the NCREIF Fund Index – Open-End Diversified Core Equity (“NFI-ODCE”). The Fund seeks to generate these returns by being disciplined in its approach to the acquisition, asset management and eventual disposition of the Fund’s investments. The Fund will acquire primarily stable properties with strong underlying credit, invest in major liquid geographic markets and property types, mitigate risk by maintaining economic diversification and actively manage properties with a view toward growing net operating income. Redemptions are available quarterly upon 45 days’ notice.
- (f) The investment objectives of the TAP Strategy are to provide an enhancement to an investor’s portfolio of financial investments and to provide a partial inflation hedge. The TAP Strategy utilizes a long-only, unleveraged portfolio of primarily exchange-traded, U.S. dollar-denominated futures and forward contracts in tangible commodities. Exchange-traded commodity groups include: agricultural, livestock, foods and fibers, energy, precious metals, and industrial metals. Redemptions are available monthly upon 5 days’ notice.
- (g) The Trumbull Property Growth and Income Fund (TPG) is a diversified Value-Add private property fund launched in June 2006. The Fund’s focus has been to invest using a broad range of value-added strategies, such as properties with expansion and/or rehabilitation potential, and to use tactical market selection to enhance returns. The Fund’s diversification strategy is based on measurements of the market basket of institutional real estate. The Fund utilizes UBS’s robust real estate research group to tactically tilt the portfolio to sectors which they perceive to be the most

attractive from a risk-return perspective. The Fund invests in the four major NCREIF property types with additional exposure to hotels, land, and debt investments. The Fund can invest up to 25% of its capital in development activities. Redemptions are available quarterly upon 60 days' notice.

- (h) Warburg Pincus Private Equity XII (the Fund) is a 2015 vintage year private equity fund that will continue Warburg Pincus' strategy of thesis driven, growth investing at scale on a global basis. The foundation of the firm's investment strategy is identifying talented entrepreneurs and management teams generally tied to a specific thesis. In addition to growth equity investments, the Fund has the ability to invest in transactions of various sizes and types, from early-stage and start-up companies to later-stage transactions that may involve leverage. Fund XII has a six year investment period and a 12 year stated life. The Fund is expected to create a diversified portfolio of 60 – 90 underlying portfolio companies with equity investments ranging from \$50 million to over \$500 million. Redemptions with the Fund are not available.

## **5. Related Party Transactions**

The Trust has a memorandum of agreement with the Virginia Local Government Finance Corporation (VLGFC), the administrator of a financial services program sponsored by the Virginia Municipal League and Virginia Association of Counties known as, "VML/VACo Finance." Under the agreement, VLGFC serves as administrator for the Trust, which operates as the "VACo/VML Pooled OPEB Trust." VLGFC receives a quarterly program fee calculated individually for each participant on a sliding scale as a percentage of invested assets. The fee covers all administrative costs including personnel, office expense, legal, accounting, and promotion, as well as a portion of investment related custodial services and investment advisory fees. The quarterly program fee during 2016 totaled \$662,461, of which custodial and investment advisory fees comprised \$183,476.

New participants pay a one-time membership fee to VLGFC upon joining the Trust and have the choice of paying a one-time membership fee of \$3,500 or a membership fee of \$500 plus an additional annual fee of 13 basis points for the first five years.

## **6. Subsequent Events**

The Trust redeemed its investment with its emerging markets equity manager, Vontobel Asset Management, following the departure of key personnel. The proceeds of the redemption were invested in the Vanguard Emerging Markets ETF until a replacement manager could be selected. Alliance Bernstein was subsequently selected to replace Vontobel at the Board of Trustees meeting held on September 9, 2016. The Board also approved an allocation to opportunistic real estate and selected UBS to manage the investment. This investment will replace the Trust's previous investment in the SPDR Dow Jones Global Real Estate ETF. The first \$7 million of the Trust's \$18 million commitment to UBS was called in October 2016.

As of September 30, 2016 the Trust had received contributions totaling \$12,487,719 from thirteen participants. The market value of net invested assets on September 30, 2016, had increased by \$43,000,979 million or 5.44%.



## **Independent Auditors' 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***

To the Board of Trustees  
Virginia Pooled OPEB Trust Fund

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 financial statements of the Virginia Pooled OPEB Trust Fund, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Virginia Pooled OPEB Trust Fund's basic financial statements, and have issued our report thereon dated November 16, 2016.

### **Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Virginia Pooled OPEB Trust Fund'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 opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Virginia Pooled OPEB Trust Fund's internal control. Accordingly, we do not express an opinion on the effectiveness of the Virginia Pooled OPEB Trust Fund'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. 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 been identified.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Virginia Pooled OPEB Trust Fund'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.

*Dixon Hughes Goodman LLP*

**November 16, 2016  
Richmond, Virginia**